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OVERSIGHT ON ISSUES RELATED TO OMB CIRCULAR A-76

HEARING BEFORE THE COMMITTEE ON VETERANS' AFFAIRS UNITED STATES SENATE NINETY-SEVENTH CONGRESS FIRST SESSION ON OMB CIRCULAR A-76

NOVEMBER 5, 1981

Printed for the use of the Committee on Veterans' Affairs



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OVERSIGHT ON ISSUES RELATED TO OMB CIRCULAR A-76

THURSDAY, NOVEMBER 5, 1981

U.S. SENATE,
COMMITTEE ON VETERANS' AFFAIRS,
Washington, D.C.

The committee met, pursuant to notice, at 9:35 a.m. in room 412, Russell Office Building, Hon. Alan K. Simpson (chairman of the committee) presiding.

Present: Chairman Alan K. Simpson (presiding), Senators Strom Thurmond, Robert T. Stafford, Bob Kasten, Jeremiah Denton, Frank H. Murkowski, Arlen Specter, Alan Cranston, Jennings Randolph, Spark M. Matsunaga, Dennis DeConcini, and George J. Mitchell.

OPENING STATEMENT OF HON. ALAN K. SIMPSON, CHAIRMAN OF THE SENATE COMMITTEE ON VETERANS' AFFAIRS

Chairman SIMPSON. The hearing will come to order.

I welcome you to these hearings on the subject of OMB Circular A-76, and its implementation within the VA's Department of Medicine and Surgery. We will be exploring the pros and cons of the contracting out of commercial and industrial type services and the specific effects that such contracting might have on the providing of medical care by the VA.

You all know that under Public Law 97-66, the Congress precluded the use of funds for medical care, medical and prosthetic research, or medical administration accounts, to carry out cost comparison studies that are a necessary part of the implementation of A-76, unless funds have been specifically appropriated for that purpose.

Our principal objective today is to determine whether such funds ought to be so appropriated. In making that determination, we will give careful attention to the cost factor, the primary justification for A-76, weighing the cost of these cost comparison studies against the potential savings to be realized. We must also consider various potential threats to the integrity of the VA health care system. Concerns have been raised about quality of performance, the accountability of a contractor's employees to the hospital's management, the employment prospects of displaced VA employees, especially those hired under Veterans' preference authorities, the possibility of a strike, and the disruption of services that it would cause, and various other management flexibility and employee morale issues.

All of those concerns will be addressed today. We must determine whether there is some compelling justification for treating the Department of Medicine and Surgery differently from other Federal agencies that are subject to A-76, something in the nature of the services provided, how they are provided and where they are provided, by whom and for whom they are provided.

And by that, I don't mean to suggest, however, that we are faced simply with a choice between going full steam ahead and crunching to a dead halt. We might well discover that there are some programs for which cost comparison studies should be funded, and others that should not.

In any event, I intend to keep a very open mind on the issue, until I have reviewed all of the arguments on both sides.

I do believe that the original policy justification for A-76 is a valid one to apply throughout the Government: That is, that when private sector performance is feasible and no overriding factors require in-house performance by Government employees, the American people and taxpayers deserve and expect the best and the most economical performance.

This consideration is not to be ignored in our consideration of the more emotional aspects of the A-76 issue. So we have a sizable number of witnesses.

Without objection, I will place in the hearing record at this point a copy of Circular No. A-76 revised, dated March 29, 1979.

[Circular No. A-76 follows:]



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

SEP 26 1980

CIRCULAR NO. A-76
Revised
Transmittal Memorandum No. 5

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Policies for Acquiring Commercial or Industrial Products and Services
Needed by the Government

1. This revision amends Transmittal Memo No. 4 to OMB Circular A-76 (revised), dated March 29, 1979. The following revisions are made to the Circular and Cost Comparison Handbook as set forth in paragraphs a through c below.

a. Calculating Contract Costs: Paragraph 9(b) of Circular A-76 is clarified by adding the following sentences: "All cost comparisons under a new start will be based on the solicitation of firm bids or offers. Prepriced option prices in existing contracts will not be used in lieu of the issuance of a new solicitation when conducting a cost comparison under a new start."

b. Utilization of Government Capacity: To ensure that all significant costs are included in the cost comparison, subparagraph F-5(g) of paragraph F-5, entitled "Utilization of Government Capacity," in Chapter V of the Cost Comparison Handbook--Supplement 1 to OMB Circular A-76 is modified as follows. Delete all references to the 5% exception so that the paragraph reads: "Computations similar to those above should also be made for the general and administrative expense rate. Similarly, the impact of contracting-out a product or service on material overhead should be determined."

c. Application of the Circular to Research and Development: The paragraph of Transmittal Memorandum No. 4, entitled "Application to R&D Activities," is amended as follows. Compliance with this Circular and the periodic review of inventoried research and development activities, except for new starts and expansions, are deferred for one additional year pending the development of appropriate criteria on determining justified "core capability." The Department of Defense (DOD), however, shall follow the statutory provision of Section 802 of the Defense Appropriation Authorization Act of FY 1980 (Public Law 96-107).

2. This revision is effective immediately and shall apply to all studies in process where no contract award has resulted.

James T. McIntyre, Jr.
James T. McIntyre, Jr.
Director



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

March 29, 1979

CIRCULAR NO. A-76

Revised

Transmittal Memorandum No. 4

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Policies for Acquiring Commercial or Industrial Products and Services Needed by the Government

Transmitted herewith is a revision of Office of Management and Budget Circular A-76, which replaces Transmittal Memorandum No. 1, dated August 30, 1967; Transmittal Memorandum No. 2, dated October 18, 1976, and Transmittal Memorandum No. 3, dated June 13, 1977.

The revised Circular (1) reaffirms the Government's general policy of reliance on the private sector for goods and services, while recognizing that (2) certain functions are inherently governmental in nature and must be performed by Government personnel, and (3) relative cost must be given appropriate consideration in decisions between in-house performance and reliance on private commercial sources. The balanced approach in this revised Circular is designed to achieve consistent policy implementation to all agencies, equitable treatment of all parties, and improved economy and efficiency in providing goods and performing services needed by the Government.

To support the increased emphasis on relative economy of Government and contract performance, a comprehensive Cost Comparison Handbook is provided as a supplement to the Circular. This Handbook is to be used by all agencies in conducting comparative cost analyses. The Handbook provides instructions for determining the total cost to Government for each alternative and will provide a more accurate basis for cost-based decisions.

This revision of Circular A-76 is the result of an extensive review of the Circular and its implementation by executive agencies, and careful consideration of all comments submitted on the draft revision that was published in August 1978. Many of those comments were accommodated through clarification and refinement of the draft. Supplementary guidance on special subjects will be developed as needed.

Application to R&D Activities

Some concern was expressed over the potential impact of the application of this Circular to Government R&D activities. While agencies with a need for in-house R&D capability can consider a "core capability" in this area as a "governmental function," additional guidance is needed to ensure some consistency in determining and justifying the size of that core capability and applying the Circular to R&D requirements, in excess of that level of capacity.

An interagency committee jointly sponsored by the Office of Federal Procurement Policy and the Office of Science and Technology Policy, has been established under the Federal Coordinating Council for Science, Engineering, and Technology, to study these issues and recommend guidelines for appropriate and uniform agency implementation. Supplemental guidance addressing R&D activities will then be developed and, after public review and comment, be issued as an amendment to the Circular. In the interim, compliance with this Circular and the periodic review of inventoried R&D activities are to be deferred for one year pending completion of the study, except for new starts and expansions, as defined in the Circular. Additional guidance will be provided on determining justified "core capability" and applying the policy to other R&D requirements to assure that essential in-house capability is maintained, and that the Government and taxpayers' interests are properly considered in contract versus in-house decisions.

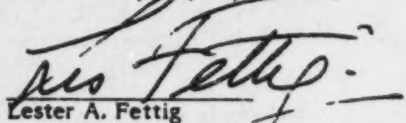
Government-Owned Contractor-Operated Activities

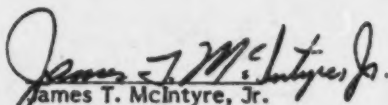
Government-owned, contractor-operated (GOCO) activities were excluded from prior issuances of the Circular. A comprehensive review of all GOCO activities is necessary to determine whether they can be completely treated under the terms of this Circular. In the interim, this Circular is to be applied only to new starts and expansions of Government-owned equipment and facilities.

Personnel Ceilings

The relationship between Circular A-76 and agency personnel ceilings was reviewed in some detail and clarified in the Circular. While it is clearly specified that agencies will not use the Circular to contract out solely to meet personnel ceilings, it is equally clear that agencies will contract out when justified under the Circular regardless of the relationship between personnel levels and authorized ceilings. Conversely, contracts for activities that are shown to be justified for in-house performance will be terminated as quickly as in-house capability can be established; when the additional spaces required cannot be accommodated within the agency's personnel ceiling, a request for adjustment will be submitted to OMB in conjunction with the annual budget review process.

The Office of Management and Budget will monitor agency implementation of this revised Circular, providing guidance and interpretations as required. Further revisions and supplements will be issued as necessary in the future to achieve the policy objectives.


Lester A. Fettig
Administrator for Federal
Procurement Policy


James T. McIntyre, Jr.
Director



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

March 29, 1979

CIRCULAR NO. A-76
Revised

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Policies for Acquiring Commercial or Industrial Products and Services Needed by the Government

1. Purpose. This Circular establishes the policies and procedures used to determine whether needed commercial or industrial type work should be done by contract with private sources or in-house using Government facilities and personnel. This Circular replaces OMB Circular No. A-76, dated August 30, 1967, and all subsequent amendments.

2. Background. In a democratic free enterprise economic system, the Government should not compete with its citizens. The private enterprise system, characterized by individual freedom and initiative, is the primary source of national economic strength. In recognition of this principle, it has been and continues to be the general policy of the Government to rely on competitive private enterprise to supply the products and services it needs.

This policy has been expressed in Bureau of the Budget Bulletins issued in 1955, 1957, and 1960. In 1966, Circular No. A-76 was issued and, for the first time, prescribed the policy and implementing guidelines in a permanent directive. The Circular was revised in 1967, by Transmittal Memorandum No. 1, to clarify some provisions and to lessen the burden of work by the agencies in implementation. Transmittal Memorandum No. 2 was issued in 1976, providing additional guidance on cost comparisons and prescribing standard cost factors for Federal employee retirement and insurance benefits.

In 1977, a comprehensive review of the Circular and its implementation was initiated. Transmittal Memorandum No. 3 was issued on June 13, 1977, announcing the review and temporarily reducing the Government retirement cost factor. This revision is the result of that review and careful consideration of comments from all interested parties.

3. Responsibility. Each agency head has the responsibility to ensure that the provisions of this Circular are followed. This Circular provides administrative direction to heads of agencies and does not establish, and shall not be construed to create, any substantive or procedural basis for any person to challenge any agency action or inaction on the basis that such action was not in accordance with this Circular, except as specifically set forth in Section 11 below.

4. Policy. This policy builds on three equally valid policy precepts:

a. Rely on the Private Sector. The Government's business is not to be in business. Where private sources are available, they should be looked to first to provide the commercial or industrial goods and services needed by the Government to act on the public's behalf.

b. Retain Certain Governmental Functions In-House. Certain functions are inherently governmental in nature, being so intimately related to the public interest as to mandate performance by Federal employees.

c. Aim for Economy; Cost Comparisons. When private performance is feasible and no overriding factors require in-house performance, the American people deserve and expect the most economical performance and, therefore, rigorous comparison of contract costs versus in-house costs should be used, when appropriate, to decide how the work will be done.

5. Definitions. For the purposes of this Circular:

a. A "Government commercial or industrial activity" is one which is operated and managed by a Federal executive agency and which provides a product or service that could be obtained from a private source. A representative, but not comprehensive, listing of such activities is provided in Attachment A. An activity can be identified with an organization or a type of work, but must be (1) separable from other functions so as to be suitable for performance either in-house or by contract; and (2) a regularly needed activity of an operational nature, not a one-time activity of short duration associated with support of a particular project.

b. An "expansion" is the modernization, replacement, upgrade, or enlargement of a Government commercial or industrial activity involving additional capital investment of \$100,000 or more, or increasing annual operating costs by \$200,000 or more; provided, the increase exceeds 20% of the total investment or annual operating cost. A consolidation of two or more activities is not an "expansion" unless the proposed total capital investment or operating cost exceeds the total from the individual activities by the amount of the threshold. An expansion which increases either capital investment or annual operating cost by 100% or more is a "new start."

c. A "conversion" is the transfer of work from a Government commercial or industrial activity to performance by a private commercial source under contract.

d. A "new start" is a newly-established Government commercial or industrial activity, including a transfer of work from contract to in-house performance. Also included is any expansion which would increase capital investment or annual operating cost by 100% or more.

e. A "private commercial source" is a private business, university, or other non-Federal activity, located in the United States, its territories and possessions, the District of Columbia, or the Commonwealth of Puerto Rico, which provides a commercial or industrial product or service required by Government agencies.

f. A "Governmental function" is a function which must be performed in-house due to a special relationship in executing governmental responsibilities. Such governmental functions can fall into several categories:

(1) Discretionary application of Government authority, as in investigations, prosecutions and other judicial functions; in management of Government programs requiring value judgments, as in directing the national defense; management and direction of the Armed Services; conduct of foreign relations; selection of program priorities; direction of Federal employees; regulation of the use of space, oceans, navigable rivers and other natural resources; direction of intelligence and counter-intelligence operations; and regulation of industry and commerce, including food and drugs.

(2) Monetary transactions and entitlements, as in Government benefit programs; tax collection and revenue disbursements by the Government; control of the public treasury, accounts, and money supply; and the administration of public trusts.

(3) In-house core capabilities in the area of research, development, and testing, needed for technical analysis and evaluation and technology base management and maintenance. However, requirements for such services beyond the core capability which has been established and justified by the agency are not considered governmental functions.

6. Scope.

a. No executive agency will engage in or contract for commercial or industrial activities except in accordance with the provisions of this Circular, or as otherwise provided by law, including, for example, Title 44 of the U.S. Code.

b. The implementation provisions of this Circular do not apply to governmental functions as defined in paragraph 5(f). These functions must be performed in-house by Government personnel.

c. This Circular applies to the need for Government ownership in any "new start" or "expansion" of a Government-owned, contractor-operated (GOCO) facility.

d. Additional provisions are as follows:

(1) This Circular does not provide authority to enter into contracts. Guidelines governing contracts for goods and services are set forth in applicable acquisition regulations.

(2) This Circular will not be used as authority to enter into contracts which establish a situation tantamount to an employer-employee relationship between the Government and individual contract personnel. Additional guidance on this subject is provided in the Federal Personnel Manual issued by the Office of Personnel Management.

(3) This Circular will not be used to justify a conversion to contract solely to meet personnel ceilings or to avoid salary limitations. When in-house performance of a "new start" is justified under this Circular but cannot be accommodated within agency personnel ceilings, an appeal for necessary adjustment to implement this Circular agency-wide should be made to OMB in connection with the annual budget review process.

(4) Major system acquisitions are governed by the provisions of OMB Circular No. A-109, "Major System Acquisitions." Reliance on the private sector is one of the general policies contained in Circular A-109 to ensure competitive consideration of all alternatives before making a decision as to the best method of satisfying an agency mission need.

(5) This Circular does not apply to consulting services of a purely advisory nature relating to the governmental functions of agency administration and management and program management. Assistance in the management area may be provided either by Government staff organizations or from private sources, as deemed appropriate by executive agencies, in accordance with executive branch guidance on the use of consulting services.

(6) This Circular applies to printing and binding only in those agencies or departments which are exempted by law from the provisions of Title 44 of the U.S. Code.

(7) This Circular should not be applied when it would be contrary to law or inconsistent with the terms of any treaty or international agreement.

7. Use of Products and Services from Other Federal Agencies.

a. Excess property and services available from other Federal agencies should be used in preference to new starts or contracts, unless the needed product or service can be obtained more economically in the private sector. This is consistent with the Federal Property and Administrative Services Act of 1949 and related regulations.

b. When a commercial or industrial activity operated by an agency primarily to meet its own needs has excess capacity, that capacity can be used to provide products or services to other agencies.

(1) If a formal program is established for managing excess capacity, such as the ADP sharing program operated by GSA, capacity that has been reported as excess can be used by other agencies with no further justification. In the absence of a formal program and report of excess capacity, another agency's use of a Government activity must be justified in accordance with paragraph 8 of this Circular. When the cost justification is used, the agency requiring the product or service will solicit competitive bids or proposals to establish commercial costs, and award a contract when more economical. The prospective providing agency will prepare the Government cost estimate, in accordance with this Circular, for comparison with the commercial cost.

(2) It is not intended that agencies create or expand capacity for the purpose of providing commercially available products or services to other agencies. When the performing agency's own requirements increase, capacity used to support other agencies is no longer excess and should be used in preference to acquisition of additional capability. Consequently, agencies should not expand a commercial or industrial activity which is providing products or services to other agencies. The user agency (or agencies) should be informed, with sufficient notice to arrange alternative sources, that the support will be terminated unless exceptional circumstances prevent that agency from finding a new source.

c. In some cases, a commercial or industrial activity is operated for the primary purpose of providing a product or service to other agencies, such as the Federal Data Processing Centers or the Office of Personnel Management training centers. All such activities must be reviewed under this Circular to determine whether continued Government operation is justified. The review should be made at the earliest possible date, but under no circumstances later than October 1, 1981. Prior to that review, agencies may use the products and services available without further justification. When continued Government operation of the activity is approved, agencies may use the products or services provided, up to the level of capability approved, with no further justification. When expansion of such an activity is proposed, the justification for approval under this Circular can be based on the entire workload, including work for other agencies.

8. Government Operation of a Commercial or Industrial Activity. Government operation of a commercial or industrial activity may be authorized under one of the following conditions.

a. No Satisfactory Commercial Source Available.

(1) A Government commercial or industrial activity can be authorized without a comparative cost analysis when it is demonstrated that:

(a) There is no private commercial source capable of providing the product or service that is needed; or

(b) Use of a private commercial source would cause an unacceptable delay or disruption of an essential agency program.

(2) Before concluding that there is no private commercial source capable of providing the needed product or service, the agency must make all reasonable efforts to identify available sources.

(a) As a minimum, the agency must place at least three notices of the requirement in the Commerce Business Daily over a 90-day period. In the case of urgent requirements, publication in the Commerce Business Daily can be reduced to two notices over a 30-day period.

(b) Agencies' efforts to find satisfactory commercial sources, especially small and minority-owned businesses, should include obtaining assistance from the General Services Administration, Small Business Administration, and the Domestic and International Business Administration in the Department of Commerce.

(3) A conclusion that use of a commercial source would not be satisfactory because it would cause an unacceptable delay or disrupt an agency program requires a specific documented explanation.

(a) Delay or disruption must be spelled out specifically in terms of cost, time and performance measures.

(b) Disruption must be shown to be of a lasting or unacceptable nature. Transitory disruption caused by conversions are not sufficient grounds.

(c) In all cases, specific explanations must be documented. If it is known that the function has been performed by contract elsewhere or at another time, the justification must specify why circumstances are substantially different.

(d) The fact that an activity involves a classified program, or is part of an agency's basic mission, or that there is a possibility of a strike by contract employees is not an adequate justification for in-house performance of that activity. Urgency by itself is not an adequate reason for starting or continuing a Government commercial or industrial activity. It must be shown that commercial sources are not able and the Government is able to provide the product or service when needed.

b. National Defense.

(1) A Government commercial or industrial activity, operated by military personnel, may be justified when:

(a) The activity or military personnel assigned are utilized in or subject to deployment in a direct combat support role;

(b) The activity is essential for training in those skills which are exclusively military in nature; or

(c) The activity is needed to provide appropriate work assignments for career progression or a rotation base for overseas assignments.

(2) A Government commercial or industrial activity providing depot or intermediate level maintenance may be justified in accordance with criteria approved by the Secretary of Defense to ensure a ready and controlled source of technical competence and resources necessary to meet military contingencies. These criteria will limit the extent of in-house capability and capacity within the military departments for depot and intermediate maintenance support of mission-essential equipment to the minimum necessary to accomplish that objective. Justification under these criteria will require a detailed explanation, on a case-by-case basis, why the needed capability cannot be supplied by:

(a) A private commercial source; or

(b) Contract operation of Government-owned facilities.

Such justification must be approved at the military department assistant secretary level or equivalent in the defense agencies.

c. Higher Cost. A Government commercial or industrial activity may be authorized if a comparative cost analysis, prepared in accordance with paragraph 9 of this Circular, indicates that the Government can provide or is providing a product or service at a lower total cost than if it were obtained from a private commercial source.

9. Cost Comparisons. A decision for in-house performance based on economy must be supported by a comparative cost analysis prepared in accordance with this Circular and the supplementing Cost Comparison Handbook.

a. Common Ground Rules.

(1) Both Government and commercial cost figures must be based on the same scope of work and the same level of performance. This requires the preparation of a sufficiently precise work statement with performance standards that can be monitored for either mode of performance.

(2) Standard cost factors will be used as prescribed by the Cost Comparison Handbook and as supplemented by agencies for particular operations. It will be incumbent on each agency to defend any variations in costing from one case to another.

(3) Cost comparisons are to be aimed at full cost, to the maximum extent practical in all cases. All significant Government costs (including allocation of overhead and indirect costs) must be considered, both for direct Government performance and for administration of a contract.

(4) In the solicitation of bids or offers from contractors for workloads that are of a continuing nature, unless otherwise inappropriate, solicitations should provide for prepriced options or renewal options for the out-years. These measures will guard against "buy-in" pricing on the part of contractors. While recompetition also guards against "buy-ins," the use of prepriced or renewal options provides certain advantages such as continuity of operation, the possibility of lower contract prices when the contractor is required to provide equipment or facilities, and reduced turbulence and disruption.

(5) Ordinarily, agencies should not incur the delay and expense of conducting cost comparison studies to justify a Government commercial or industrial activity for products or services estimated to be less than \$100,000 in annual operating costs. Activities below this threshold should be performed by contract unless in-house performance is justified in accordance with paragraph 8.a. or b. However, if there is reason to believe that inadequate competition or other factors are causing commercial prices to be unreasonable, a cost comparison study may be conducted. Reasonable efforts should first be made to obtain satisfactory prices from existing commercial sources and to develop other competitive commercial sources.

(6) The cost comparison will use a rate of 10% per annum as the opportunity cost of capital investments and of the net proceeds from the potential sale of capital assets, as prescribed in the Cost Comparison Handbook.

b. Calculating Contract Costs.

(1) The contract cost figure must be based on a binding firm bid or proposal, solicited in accordance with pertinent acquisition regulations. Bidders or offerors must be told that an in-house cost estimate is being developed and that a contract may or may not result, depending on the comparative cost of the alternatives.

(2) The factor to be used for the Government's cost of administering contracts, in addition to other costs of using contract performance as specified in the Handbook, is 4% of the contract price or expected cost.

c. Calculating Costs of Government Operation.

(1) Each agency should assure that Government operations are organized and staffed for the most efficient performance. To the extent practicable and in accordance with agency manpower and personnel regulations, agencies should precede reviews under this Circular with internal management reviews and reorganizations for accomplishing the work more efficiently, when feasible.

(2) The Government cost factor to be used for Federal employee retirement benefits, based on a dynamic normal cost projection for the Civil Service Retirement Fund, is 20.4%.

(3) The Government cost factor to be used for Federal employee insurance (life and health) benefits, based on actual cost, is 3.7%.

(4) The Government cost factor to be used for Federal employee workmen's compensation, bonuses and awards, and unemployment programs is 1.9%.

d. An existing in-house activity will not be converted to contract performance on the basis of economy unless it will result in savings of at least 10% of the estimated Government personnel costs for the period of the comparative analysis.

e. A "new start" will not be approved on the basis of economy unless it will result in savings compared to contract performance at least equal to 10% of Government personnel costs, plus 25% of the cost of ownership of equipment and facilities, for the period of the comparative analysis.

f. All cost comparisons must be reviewed by an activity independent of the cost analysis preparation to ensure conformance to the instructions in the Cost Comparison Handbook.

10. Administering the Policy.

a. Implementation.

(1) Each agency will designate an official at the assistant secretary or equivalent level, and officials at subordinate contact points for major components, to have overall responsibility for implementation of this Circular within the agency.

(2) Each agency will establish one or more offices as central points of contact to maintain cognizance of specific implementation actions. These offices will have access to all decision documents and data pertinent to actions taken under the Circular and will respond, in a timely manner, to all requests concerning inventories, schedules, reviews, and results of reviews. In considering requests which include information supplied by contractors or prospective contractors, agencies will be guided by OFPP Policy Letter No. 78-3, "Requests for Disclosure of Contractor-Supplied Information Obtained in the Course of a Procurement."

(3) Within 90 days after the date of issuance, each agency will promulgate this Circular, with the minimum necessary internal instructions, identifying the designated official and the central and subordinate contact points. When issued, copies of the internal instructions will be forwarded to OMB's Office of Federal Procurement Policy for review. Copies of subsequent changes will also be forwarded for review.

(4) Each agency will recognize that work for the Federal Government may be performed by use of military personnel, civilian employees, and contract services, and that past experience demonstrates that all three methods have been responsive and dependable in performing sensitive and important work.

(5) Each agency will ensure that contracts awarded as a result of reviews under Circular A-76:

(a) Contain all applicable clauses and provisions related to equal employment opportunities, veterans' preference, and minimum wages and fringe benefits, including implementation of OFPP Policy Letter No. 78-2, dated March 29, 1978, relating to "wage busting;"

(b) Include a provision, consistent with Government post employment conflict of interest standards, that the contractor will give Federal employees, displaced as a result of the conversion to contract performance, the right of first refusal for employment openings on the contract in positions for which they are qualified;

(c) Are awarded to a responsible and responsive bidder or offeror, as required by applicable acquisition regulations; and

(d) Are administered and monitored to achieve proper performance, using appropriate contractual remedies any time performance is less than satisfactory.

(6) Each agency will exert maximum effort to find suitable employment for any displaced Federal employees, including:

(a) Giving them priority consideration for suitable positions with the Government;

(b) Paying reasonable costs for training and relocation when these will contribute directly to placement;

(c) Arranging for gradual transition when conversions are made to provide greater opportunity for attrition and placement; and

(d) Coordinating with the Department of Labor and other agencies to obtain private sector employment for separated workers.

(7) Each agency will provide for alterations to the mode of performance to be timed in consonance with, and adjusted for, the budget process to the extent required and consistent with the firm bid cost study approach.

b. Inventories. Each agency will immediately compile a complete inventory of all commercial and industrial activities subject to this Circular.

(1) Agencies will prepare and maintain a complete inventory of all individual commercial or industrial activities (as defined in paragraph 5.a.), which they operate. In addition to general descriptive information, the inventory should include for each activity: the amount of the Government's capital investment, the annual cost of operation, the date the activity was last reviewed, and the basis on which the activity is being continued under this Circular. The inventory will be updated at least annually to reflect the results of reviews as conducted.

(2) Agencies will also prepare and maintain an inventory of all contracts in excess of \$100,000 annually, except those awarded under a duly authorized set aside program, for services which the agency determines could reasonably be performed in-house, including any activities that have been converted from in-house to contract performance. In addition to general descriptive information, the inventory will include: the contract number, name of the contractor, contract period, period of any options, and the total contract price or estimated cost. Inventory updates will reflect exercise of options and the termination and award of contracts.

c. Reviews. Agencies will prepare a detailed schedule for the review of each commercial or industrial activity and contract in the inventory to determine if the existing performance, in-house or contract, continues to be in accordance with the policy and guidelines of this Circular. The flow chart provided as Attachment B demonstrates the sequence of actions required for proper implementation of the Circular.

(1) The schedule for review of in-house commercial and industrial activities will provide for review of all activities during the three-year period following issuance of this revised Circular. Consideration should be given first to criteria that do not concern cost. Unless continuation is justified under paragraphs 8.a. or b., a cost comparison must be conducted to determine the relative cost of Government and private performance.

(2) The schedule for review of contracts will show the date that each contract (including options) will expire, and the date that the requirement will be reviewed to determine if contract performance is to be continued. The agency will review the contract cost and determine whether it is likely that the work can be performed in-house at a cost that is less than contract performance by 10% of Government personnel costs plus 25% of the cost of ownership of equipment and facilities. When this is determined to be likely, a cost comparison will be conducted.

(3) Both schedules will be completed and provided to the Office of Federal Procurement Policy, OMB, within 120 days of the date of issuance of this Circular. These schedules will be made available by the agency to all potentially affected employees and their representatives, and published for the information of contractors.

(4) Reviews will be conducted in accordance with the schedules, unless it is determined that a change in the schedule will be in the best interest of the Government. In such cases, after approval by the agency head or his designee, the schedule can be revised with 60 days notice to all affected parties.

(5) After the initial review, activities approved for continuation will be reviewed again at least once every five years. When it is determined by the agency head or his designee that the circumstances which supported the initial approval are not subject to change, subsequent reviews may be waived. These activities will be retained in the inventory, however, and so identified. A copy of the justification and the waiver will be made available to all interested parties upon request to the agency contact point.

(6) When a proposed expansion, modernization, or upgrade exceeds the threshold for capital investment or operating costs, it will be reviewed as though it were a scheduled review of an existing activity. At least 60 days notice will be given to all affected parties.

(7) When the number of commercial and industrial activities and the number of covered contracts is so great that reviews cannot be completed in the prescribed time period, the agency may request approval from the Office of Federal Procurement Policy, OMB, to schedule the reviews over a longer period.

d. New Starts.

(1) A new start should not be initiated by an executive agency unless the justification for establishing the activity under the provisions of this Circular has been reviewed and approved by a senior official of the agency. A new start which involves a capital investment or annual costs of \$500,000 or more must be approved by the agency head or by an official at the assistant secretary or equivalent level.

(2) The actions to be taken under this Circular should normally be completed before the agency's budget request is submitted to OMB. Data in support of such budget requests will be submitted in accordance with OMB Circular No. A-11. In the case of a proposed new start involving a major capital investment where the item to be acquired requires a long lead time (e.g., ADP system, building), approval of budget resources will not constitute OMB approval of that method of meeting the agency need. A final determination to initiate the new start or to rely on a private commercial source, within the resources approved, will be made in accordance with this Circular and other applicable policies, prior to any commitment to a particular acquisition strategy.

(3) When Government ownership of facilities is necessary, the possibility of contract operation must be considered before in-house performance is approved as a new start. If justification for Government operation is dependent on relative cost, the comparative cost analysis may be delayed to accommodate the lead time necessary in acquiring the facilities.

(4) When in-house performance to meet a new requirement is not feasible, or when contract performance would be under an authorized set-aside program, a contract can be awarded without conducting a comparative cost analysis.

e. Set-Aside Programs

(1) It is the general policy of the Government, as expressed in the Small Business Act, to ensure that small businesses, including those owned and managed by disadvantaged persons, receive a fair share of Government contract awards.

(2) Consequently, contracts awarded under authorized set-aside programs will not be reviewed for possible in-house performance. Additionally, new requirements which would be suitable for award under a set-aside program should be satisfied by such a contract without a comparative cost analysis.

(3) On the other hand, in-house activities (in excess of \$100,000 annually) will not be considered for performance under a set-aside contract except when the conversion is justified by a comparative cost analysis.

11. Appeals.

a. Each agency will establish a procedure for an informal administrative review of determinations made under this Circular. This procedure will only be used to resolve questions of the determination between contract and in-house performance, and will not apply to questions concerning award to one contractor in preference to another contractor. Upon written request from a directly affected party raising a specific objection, the appeals procedure will provide for:

(1) An independent, objective review of the initial determination and the rationale upon which the decision was based.

(2) An expeditious determination, within 30 days, made by an official at the same or higher level than the official who approved the original decision.

b. The appeals procedure is to provide an administrative safeguard to assure that agency decisions are fair, equitable, and in accordance with established policy. This procedure not authorize an appeal outside the agency or a judicial review.

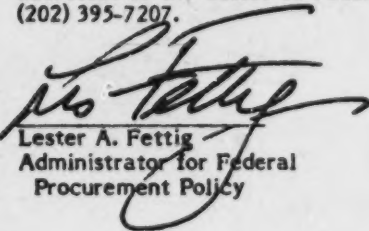
c. Since the appeal procedure is intended to protect the rights of all affected parties -- Federal employees and their representative organizations, contractors and potential contractors, and contract employees and their representatives -- the procedure and agency determinations may not be subject to negotiation, arbitration, or agreements with any one of those parties. Agency decisions are final.

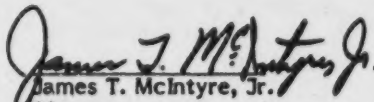
d. Agency appeal procedures, when issued, will be submitted to OFPP for review pursuant to paragraph 10.a.(3).

12. Effective Date.

This Circular is effective May 1, 1979, but need not be applied to studies in process where a solicitation for contract bids or proposals was issued prior to the effective date.

Questions or inquiries about this Circular or its implementation should be addressed to the Office of Federal Procurement Policy, OMB, telephone number (202) 395-7207.


Lester A. Fettig
Administrator for Federal
Procurement Policy


James T. McIntyre, Jr.
Director

ATTACHMENT A

EXAMPLES OF COMMERCIAL AND INDUSTRIAL ACTIVITIES

Audiovisual Products and Services

Photography (still, movie, aerial, etc.)
Photographic processing (developing, printing, enlarging, etc.)
Film and videotape production (script writing, direction, animation,
editing, acting, etc.)
Microfilming and other microforms
Art and graphics services
Distribution of audiovisual materials
Reproduction and duplication of audiovisual products

Automatic Data Processing

ADP services -- batch processing, time-sharing, etc.
Programming and systems analysis, design, development, and
simulation
Key punching and data entry services
Systems engineering and installation
Equipment installation, operation, and maintenance

Maintenance, Overhaul, and Repair

Aircraft and aircraft components
Ships, boats, and components
Motor vehicles
Combat vehicles
Railway systems
Electronic equipment and systems
Weapons and weapon systems
Medical and dental equipment
Office furniture and equipment
Industrial plant equipment
Photographic equipment
Space systems

Systems Engineering, Installation, Operation, and Maintenance

Communications systems -- voice, message, data; radio, wire,
microwave, and satellite
Missile ranges
Satellite tracking and data acquisition
Radar detection and tracking
Television systems -- studio and transmission equipment,
distribution systems, receivers, antennas, etc.
Recreational areas
Bulk storage facilities

Manufacturing, Fabrication, Processing, and Packaging

- Ordnance equipment
- Clothing and fabric products
- Liquid, gaseous, and chemical products
- Logging and lumber products
- Communications and electronics equipment
- Rubber and plastic products
- Optical and related products
- Sheet metal and foundry products
- Machined products
- Construction materials
- Test and instrumentation equipment

Real Property

- * Design, engineering, construction, modification, repair, and maintenance of buildings and structures
- Construction, alteration, repair, and maintenance of roads and other surfaced areas
- Landscaping, drainage, mowing and care of grounds

Industrial Shops and Services

- Machine, carpentry, electrical and other shops
- Industrial gas production and rectifying
- Equipment and instrument fabrication, repair and calibration
- Plumbing, heating, electrical, and air conditioning services, including repair
- Fire protection and prevention services
- Custodial and janitorial services
- Refuse collection and processing

Health Services

- Surgical, medical, dental, and psychiatric care
- Hospitalization, outpatient, and nursing care
- Physical examinations
- Eye and hearing examinations -- manufacturing and fitting glasses and hearing aids
- Medical and dental laboratories
- Dispensaries
- Preventive medicine
- Dietary services
- Veterinary services

Transportation

- Operation of motor pools
- Bus service
- Vehicle operation
- Air transportation
- Water transportation
- Trucking and hauling

Printing and Reproduction

- Printing and binding -- where the agency or department is exempted from the provisions of Title 44 of the U.S. Code
- Reproduction, copying, and duplication
- Blue-printing

Research and Development

- Basic research
- Applied research
- Development
- Concept formulation and demonstration
- R&D studies
- R&D testing
- R&D support services

Office Services

- Stenographic recording and transcribing
- Word processing/data entry
- Mail/messenger
- Translation
- Information systems and distribution
- Financial auditing and services
- Management auditing

Security

- Guard and protective services
- Systems engineering, installation, and maintenance of security systems and individual privacy systems
- Forensic laboratories

Food Services

- Operation of cafeterias, mess halls, kitchens, bakeries, dairies,
and commissaries
- Vending machines
- Ice and water

Other Services

- Laundry and dry cleaning
- Library operation
- Mapping and charting
- Architect and engineer services
- Geological surveys
- Cataloging
- Training -- academic, technical, vocational, and specialized (within the
limitations of P.L. 85-507, unless waived by the Office of Personnel
Management)
- Operation of utility systems (power, gas, water, steam, and sewage)

[illegible]

Chairman SIMPSON. This is a deviation from our usual format, but Senator Stafford must leave to introduce his State's Governor at a hearing, and I know my good colleague from California, Senator Cranston, will understand. I would recognize Bob Stafford for a moment before—

Senator CRANSTON. Of course.

Senator STAFFORD. Thank you very much, Mr. Chairman, and Alan. I appreciate the courtesy, and I ask unanimous consent that my statement may appear in the record after that of Senator Cranston. [See p. 39.]

Chairman SIMPSON. I now recognize my fine colleague from California, Senator Al Cranston.

Senator CRANSTON. Thank you very much. Before proceeding, I'd like to introduce a longtime friend and associate of mine, who is here today in case we need any magic in dealing with veterans' problems.

His name is Lee Falk, and he's the creator of "Mandrake the Magician" and "The Phantom" two cartoon strips that many of you may follow. You can follow "The Phantom" in the only remaining newspaper we now have in Washington, D.C.

Lee Falk.

Mr. FALK. Thank you. It's a pleasure. [Applause.]

Chairman SIMPSON. Al, let me say, in my ninth year of life I referred to that comic strip, oh, I loved that one—I called it "Mandrack [sic] the Magician." I remember that. I was not quite correct, but I was a great fan. Thank you so much.

Senator CRANSTON. Now how's the stenographer going to get that into the record? [Laughter.]

Chairman SIMPSON. Spell it out.

Senator CRANSTON. I welcome the many witnesses that are here today for this hearing on the impact of the implementation of OMB Circular A-76, on the Veterans' Administration, especially on the VA's Department of Medicine and Surgery.

I look forward to hearing your testimony as the committee attempts to come to terms with the potential impact of the circular.

The issue before us is a complex one. As attention has been focused on the implementation of Circular A-76 in the VA, there's been a tendency recently to paint the issue in very stark terms. I suspect, however, that this is not an either-or issue. Rather, I anticipate that there is some role for greater contracting by the VA with the private sector for certain commercial or industrial activities and that this opportunity may extend into DM&S.

I am equally certain, however, that the VA cannot and should not launch headlong into wide-scale contracting-out activities before the Congress has thoroughly analyzed the issues involved. The very cost of the studies, in both dollars and personnel hours, that would have to be undertaken in DM&S before contracting-out decisions are made, is ample reason during this time of severe budgetary and personnel constraints for the Congress to insist that there be a much greater degree of understanding of the many ramifications of Circular A-76 before any full-scale implementation in DM&S.

That is why the Democratic members of the committee recommended to the chairman on September 22, that the compromise

agreement on S. 917, the veterans' comp bill, then under negotiations between the Houses, be amended to include a provision, precluding the use of any VA health care appropriations to carry out any studies regarding contracting out, such as required by Circular A-76. Thanks to the cooperation and good work of my good friend, Al Simpson, and our counterparts in the House committee, Sonny Montgomery and John Paul Hammerschmidt, that provision was enacted as section 601(b)(2) of Public Law 97-66.

I want to thank you, Al, for your prompt response to our letter calling for the scheduling of today's A-76 hearing. The chairman's actions in this regard are another good example of the close cooperation and accommodation that has characterized our very good personal relationship from the very start.

I believe that the committee must undertake a thorough evaluation of this issue, and I view today's hearings as an important step in that process.

I would like to touch briefly on a few points I think must be addressed by the committee as we undertake this evaluation of Circular A-76. I believe that any projected gains from the A-76 process, whether fiscal or in furtherance of the underlying philosophy of the circular, that the Government should not compete with its citizens, must be measured against the impact of the contracting-out process in two general areas: Namely, the VA's ability to provide benefits and services, most particularly quality medical care services, and fairness and due consideration for VA employees. The VA health-care system is the area of the VA most susceptible to change through Circular A-76, simply because the vast majority of VA employees are employed in DM&S, and also because providing health care is a very labor-intensive undertaking.

I believe that the VA's General Counsel, in an opinion dated March 21, 1980, was absolutely correct in his conclusion that there is a "national policy to provide, as a governmental function, a complete medical and hospital service for our Nation's veterans." Indeed, the U.S. District Court for the District of Oregon recently endorsed this position in the case of Coalition for Better Veterans Care, Inc., versus the Administrator of Veterans' Affairs. If this premise is accepted—and I believe it must be—the question that must be addressed is the degree to which the various functions currently performed within DM&S are lawfully and appropriately susceptible to contracting out.

At one end of the spectrum, it is easy to determine that it would be improper to apply A-76 so as to contract for the functions currently performed by VA health-care professionals and others providing direct, hands-on health-care services and by managerial personnel.

Toward the other end of the spectrum, where various job functions within DM&S are less directly tied to providing health care, the answers are less clear. I believe that the committee must develop the best possible understanding of the relationship of other functions within DM&S—such as food services—to the Department's ability to fulfill its primary mission of providing quality health care to eligible veterans.

As I noted earlier, the other area of concern that I have regarding Circular A-76 is its impact on current VA employees. My con-

cerns in this regard are both short and long term. In the short term, I believe that it is critical that we not lose sight of the fact that a goal of Circular A-76 is to reduce the number of Government employees.

Although much of the discussion on this point often seems to take place on a theoretical plane, the positions that would be eliminated are filled by real people, who, in the vast majority of cases, are loyal, hard-working Government employees, and we need to understand and evaluate fully the impact of the implementation of Circular A-76 on these individuals.

If Government positions are eliminated, what protection and assistance will be provided to those now holding the jobs? Will they be employed elsewhere by the Government? By the contractor who takes over the function? What will happen to their retirement benefits, their health-care coverage? These are important questions to which I believe the committee needs answers before we support implementation of the A-76 process in DM&S.

In this regard, I think it's important that we recognize that just the present discussion regarding Circular A-76 is reported to be having a serious impact on employee morale. How much greater and widespread will that impact be if the process gets underway, and what are the implications that such morale problems have for patient care?

My long-term concerns relating to the VA employees center on the ability of the system to continue to provide quality health care if significant numbers of those performing work in the system no longer owe any allegiance to the VA. I believe that this is a very significant concern that must be addressed before the Congress endorses any further action in the VA on Circular A-76.

Additionally, and very importantly, I am concerned that contracting out would nullify the advances we've made over the years in the employment of veterans, particularly those with service-connected disabilities and those from the Vietnam era—much of which is by the VA—through veterans' preference, VRA appointments, and other provisions facilitating Federal employment of veterans.

A final long-term question I have about this Circular A-76 process is how far the administration may be planning to push this emphasis. Attachment "A" of the Circular, which provides examples of activities within the scope of the Circular, lists—with no specific expression of special limitation or conditions—"health services," including for example, "surgical, medical, dental, and psychiatric care; hospitalization, outpatient, and nursing care." This indicates that virtually the entire DM&S system should be considered for contracting out. Is this really what is being proposed?

Until October 23, I felt that it couldn't really be, but my concerns have been heightened by a statement explaining the President's proposed deferral—D82-140—of appropriations for five VA major construction projects that was forwarded to the Congress on that date.

It was there stated that the funds were deferred while the administration, "considers alternative methods for providing readily available, quality medical care for eligible veterans."

Now, the only alternative to the provision of care through VA facilities that has been under consideration within the administra-

tion is to provide veterans' health care by way of a voucher system—so-called mainstreaming—under which veterans would receive health care in non-VA hospitals and the Federal Government would pay for the care received.

By whatever name it is called, this is clearly the ultimate "contracting-out" of VA health-care functions, and would in my view inevitably lead to the true demise of the VA health-care system.

The fact that such an approach is under active consideration by the administration at this time should give all of us in the Congress reason to pause and reflect very seriously on the extent to which Circular A-76 should be implemented by the VA.

I also want to note that with reference to this deferral of major construction funding, I will today introduce on behalf of a number of Senators an impoundment resolution, disapproving the deferral, in order to make clear that the Congress rejects this stated justification. I intend to press for swift Senate passage of this resolution to demonstrate our overwhelming opposition to the suggestion that there is any appropriate role for the concept of "mainstreaming" or "vouchering out" veterans' health care. And I would welcome the cosponsorship of each member of this committee. Frankly, I view the resolution as a true watershed—a continental divide, if you will—affording the Senate the clear opportunity, at this critical point in the history of the VA health-care system, at this time of extreme budgetary constraints, to stand up and say, in an entirely bipartisan way, and I want it to be that, that it totally rejects the notion that any part of the Federal Government should consider the dismantling of that system and the creation of a voucher system to replace it.

Mr. Chairman, I ask that the September 22 A-76 letter, and appropriate excerpts from the other September 22 letter that I referred to earlier, as well as the VA General Counsel's opinion, and appropriate excerpts from the President's October 23 message and deferral D82-140, be printed at this point in the hearing record, and I thank you.

Chairman SIMPSON. Without objection, that is so ordered.

[The September 22, 1981 A-76 letter; the appropriate excerpts from the September 22, 1981 letter regarding the proposed compromise agreements; the VA General Counsel's opinion; and the appropriate excerpts from President Reagan's October 23, 1981 message and deferral D82-140; follow:]

ALAN K. SIMPSON, WFO, CHAIRMAN
 STANLEY THOMAS, S.C.
 JIMMY T. STAFFORD, VT.
 ROBERT W. HARTEN, JR., WIS.
 JENNIFER DENTON, ALA.
 PHILIP H. HARRINGTON, ALABAMA
 ARLEN SPOFFORD, PA.
 ROBERT F. CENNETT, CHIEF CLERK

ALAN GRANITZ, CALIF.
 JENNIFER DENTON, ALA.
 PHILIP H. HARRINGTON, ALABAMA
 ROBERT F. CENNETT, CHIEF CLERK

SEP 22 1981

United States Senate

COMMITTEE ON VETERANS' AFFAIRS
 WASHINGTON, D.C. 20510

September 22, 1981

Honorable Alan K. Simpson
 Chairman
 Committee on Veterans' Affairs
 United States Senate
 Washington, D.C. 20510

Dear Al,

As you know, on July 29, the Veterans' Administration published in the Federal Register a schedule setting forth a timetable for VA action to "study certain commercial-industrial type activities" (CITAs) in the Department of Medicine and Surgery (DM&S) as part of the agency's compliance with OMB Circular A-76.

We recognize that there is a need to find economies in the VA budget, but we are concerned that there are many questions about the impact of OMB Circular A-76 on DM&S that should be answered before the VA goes forward in the manner anticipated by that Circular with wide-scale and very costly (some estimates are as high as \$29 million) surveys of the feasibility of contracting out functions currently performed by DM&S employees. Among the questions that we believe must be answered satisfactorily are ones concerning the impact on the overall ability of DM&S to fulfill its various missions, especially its primary mission of providing quality health care to eligible veterans and, in fact, whether A-76, as applied to those functions of DM&S that relate directly to this primary mission, is consistent with the statutory responsibilities of DM&S set forth in title 38. In an opinion issued on March 21, 1980, the VA's General Counsel ruled that, in light of the specific statutory structure and functions of DM&S, "the application of A-76 to the basic medical care operations of DM&S cannot be justified legally"

As an example of the possible impact of Circular A-76 on DM&S, one of the CITAs that was listed for review in the schedule published in the Federal Register was food services, including preparation and delivery services. Many persons familiar with the DM&S system and with other health-care systems generally have suggested very persuasively that a medical center's dietetics service is an integral part of the health-care system and, thus, have questioned the result of such a contracting in terms of effective management of overall health care.

Questions have also been raised about the agency's ability to provide uninterrupted health care to eligible veterans if some, many, or most important functions were carried out by an outside contractor and the contractor became unable to provide the contracted services because of an employee work action, such as a strike, a result that is forbidden by current law. Another concern that has been raised about the impact of Circular A-76 is the possibility that once the agency contracts with

a private entity for a service it will lose the capacity to perform the function in-house itself; in areas where there is only one qualified contractor available, that contractor would be in a position to demand increasingly greater fees for performing the function. We have received reports of such situations that have already occurred but have not yet had the opportunity to verify them.

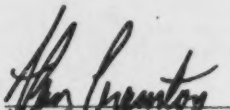
Among those expressing concerns to us about Circular A-76 have been VA employees, both individually and collectively. We have also heard from organizations representing these employees. Naturally, many employees have expressed legitimate concerns about the impact of Circular A-76 on their own positions. Many also have raised larger concerns about the VA's overall ability to provide quality health care when many of the providers lack employee identification with or loyalty to the system.

Hence, we strongly question whether the initial phase of the agency's compliance with Circular A-76, as set forth in the Federal Register notice, in view of the very significant investment of funds, time, and effort that will be required, is warranted until there is a more complete understanding of whether and to what extent DM&S is being legally and properly required to comply with Circular A-76.

In light of these and other concerns, we strongly urge that the Committee hold at least one day of oversight hearings in October at which the Administration, including representatives of OMB involved with Circular A-76, veterans and veterans' organizations, VA employees and organizations who represent these employees, and others concerned could testify.

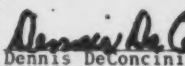
With warm regards,

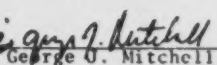
Cordially,


Alan Cronston

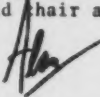

Jennings Randolph


Spark M. Matsunaga


Dennis DeConcini


George C. Mitchell

P.S. I know that your schedule for the remainder of this session will be quite tight because of your responsibilities in connection with the immigration issue and, if you decide to schedule this hearing, I would be willing to see if I could chair at least part of the hearing.



ALAN K. SIMPSON, WYO. CHAIRMAN
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 RICHARD T. STAFFORD, VT.
 ROBERT W. SALTER, ID., VICE
 JENNIFER DENTON, ALA.
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ALAN CAMPBELL, CALIF.
 JENNIFER BANCROFT, W. VA.
 SPENCER H. BATHURST, MARYLAND
 DENNIS DE CONCH, MISS.
 ROBERT J. GIVENELL, MAINE

United States Senate

COMMITTEE ON VETERANS' AFFAIRS
 WASHINGTON, D.C. 20510

September 22, 1981

Honorable Alan K. Simpson
 Chairman
 Committee on Veterans' Affairs
 United States Senate
 Washington, D.C. 20510

Dear Al,

In connection with your forthcoming meeting with Sonny Montgomery on H.R. 3499 and S. 917, I am writing on behalf of the Democratic membership of the Committee to express our general support for the proposed compromise agreements worked out on those measures and to urge that our Committee give its prompt approval to these compromises so that final Congressional action can be taken and the bills sent to the President.

It is our understanding that you and/or the Office of Management and Budget have reservations about five provisions in the proposed agreements. Our views on each provision follow:

* * * * *

2. S. 917: Section 401 of H.R. 3995 and section 601 of the proposed compromise agreement -- Subjecting Major VA Reorganizations to Congressional Review. This House provision had its genesis in the Administration's proposal of March 10 to close numerous VA Regional Offices and reduce benefits personnel by 3,300 over the next two fiscal years. Although our Committee's opposition to this far-reaching reorganization and the opposition of House Committee members, particularly Sonny Montgomery, were effective in gaining, in the context of the Gramm-Latta budget compromise, a postponement of this proposal from OMB, the Administration's retreat from its position on the VA budget (see item 1) highlights the need for such a provision.

We believe that it is reasonable and appropriate for the Congress to insist on some role in consideration of major reorganizations of programs designed to assure the effective implementation of entitlement and other benefits provided to veterans in return for faithful service to the Nation. We further believe that the compromise -- providing that either Committee on Veterans' Affairs can assure, by expressing its approval, that a proposed reorganization proceeds regardless of the view in the other body (as compared to the House-passed provision allowing either House to block a reorganization) -- appropriately protects prerogatives in a Congress with split party leadership and is also fair to the Administration's viewpoint by giving a strong presumption of regularity to Executive Branch proposals.

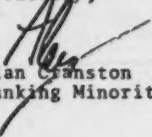
Moreover, we believe the Senate should propose a further modification in this provision to deal with the very costly (some estimates are as high as \$29 million) OMB Circular A-76 process requiring movement toward more contracting for services now performed by VA Department of Medicine and Surgery (DM&S) employees. That process is now underway in DM&S facilities, which are being required to conduct enormous numbers of studies regarding the possibility of contracting out certain of their major functions despite the VA General Counsel's opinion that such contracting is not consistent with the statutory responsibilities of DM&S under title 38. (The A-76 process is the subject of a separate letter to you.) Given the questionable legality of the application of A-76 in DM&S, the many serious substantive concerns and questions that have been raised about the impact of extensive A-76 contracting on the effectiveness and continuity of the VA health-care system, and the substantial cost and resource allocation implications of the VA's present schedule of A-76 reviews, we urge that the bill be amended to prohibit the expenditure of appropriations and the activities of VA employees in connection with the A-76 survey process unless funds are expressly appropriated by Congress for this specific purpose.

* * * * *

We very much hope you will give our views the most serious consideration prior to and in your meeting with Chairman Montgomery.

With warmest regards,

Cordially,


Alan Cranston
Ranking Minority Member

cc: Honorable Jennings Randolph
Honorable Spark M. Matsunaga
Honorable Dennis DeConcini
Honorable George J. Mitchell

UNITED STATES GOVERNMENT

Memorandum

DATE MAR 21 1980

TO Chief Medical Director (13)

FROM General Counsel (023)

SUBJ Draft of VA Circular 00-79 Policies for acquiring commercial or industrial products and services needed by the government

1. You have requested our opinion regarding the application of OMB Circular A-76 dated March 29, 1979, to Department of Medicine and Surgery (DM&S) activities. Circular A-76 prescribes "Policies for acquiring Commercial or Industrial Products and Services Needed by the Government." Because attachment "A" to the circular lists among its other examples of commercial and industrial activities, health services of almost every kind, your question and concerns are well founded.

2. In attempting to reach a rational understanding of the application of the circular to DM&S operations, certain concepts fundamental to the operation of our system of Government must be considered. First, the President and the executive branch of the Government administer laws enacted by the legislative branch of the Government. Thus, any Executive order or other Presidential directive issued in carrying out the responsibility of the executive branch to administer the laws must be consistent with the law being administered. Second, when Congress enacts a law specifically directing an agency in the executive branch to take a prescribed course of action, that law is generally deemed to preempt the field.

3. In applying Circular A-76 to DM&S activities, careful attention must be given to the specific language and intent of the circular, itself, and the accompanying transmittal memorandum. In that transmittal memorandum it is stated that the circular reaffirms the general policy of relying on the private sector for goods and services, while recognizing that certain functions are inherently governmental in nature and must be performed by Government personnel. The transmittal memorandum also points out that in those areas not inherently governmental in nature, relative cost must be given appropriate consideration in making decisions between in-house performance and contracting out. The circular reiterates the basic premise that in a democratic free economic system, the Government should not compete with its citizens and, thus, follows the general policy of relying on competitive private enterprise to supply the products and services it needs. Bulletins and circulars of OMB have articulated this policy in 1955, 1957, 1960, 1966, 1967 and 1976, before this latest version in 1979.



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VA FORM 2105
AUG 1979

2.

Chief Medical Director (13)

4. In defining the scope of the circular, OMB in paragraph 6.b. has specifically exempted governmental functions which are defined in paragraph 5(f) as a function "which must be performed in-house due to a special relationship in executing governmental responsibilities." Categories of such functions include "[d]iscretionary application of Government authority . . . as in management of Government programs requiring value judgments, as in directing the national defense; . . . selection of program priorities"

5. Given the fundamental concepts of our form of Government discussed above, the language discussing the intent of the circulars, the history of OMB pronouncements on contracting out, and the language of the latest circular relating to its scope, we believe it abundantly clear that the basic provision of health care by DM&S is not significantly impacted by the latest version of OMB Circular A-76.

6. Under current statutes, OMB cannot direct the VA to contract out its basic health care function. The Congress in enacting Public Law 79-293 preempted this field when it created in the VA a DM&S under a Chief Medical Director, having as its primary (i.e., governmental) function to provide a complete medical and hospital service for the care and treatment of veterans. This is a national policy established by the Congress, and can be changed only by the Congress. Indeed, President Carter's letter of August 27, 1979, to Senator Alan Cranston recognized this and voiced the President's continuing support for such policy.

7. Moreover, we believe that Congress, in establishing specific authority for certain limited types of contracting by DM&S, was clearly aware of the general restrictions on contracting authority within DM&S. That the contracting out policy under title 38 is separate and distinct from that of Circular A-76 is given clear expression in section 621 of title 38 which authorizes the Administrator to prescribe: (1) rules and procedures governing furnishing of hospital, nursing home and domiciliary care and (2) limitations in connection with the furnishing of such care. Chapter 17 of title 38 sets forth in detailed provisions the Department's role as a direct provider of hospital, nursing home, domiciliary, and medical care. By its terms chapter 17 poses specific restrictions on contracting for the provision of those services. In qualifying the scope of the VA's authority to furnish those modes of care to eligible veterans, the statute has long

3.

Chief Medical Director (13)

provided that such services could only be furnished "within the limits of VA facilities." VA facilities were defined in chapter 17 to include private facilities with which the VA may contract. But such authority is available only for very limited classes of beneficiaries. There has long been a specific limitation on fee-basis care, for example, particularly where it involves care for a nonservice-connected condition. Furthermore, in Pub. L. No. 94-581, Congress, in responding to the rapid growth of VA fee-basis medical care, imposed still further limits on such contract care. The authorizing committee which reported out the legislation that formed the core of Pub. L. No. 94-581 described the amendment as making clear "that the VA may contract for fee-basis service only when VA or other Federal hospitals or clinics 'are not capable of furnishing economical care because of geographical inaccessibility or of furnishing the particular type of care or services required.'" The effect of this new language is to limit the authorization of fee-basis service for service-connected or nonservice-connected disabilities to those situations when regular VA hospitals and clinics (or other Federal facilities) are genuinely unable to provide the needed services themselves." SEN. REP. NO. 94-1206, 94th Congress, 2d Session, p. 75.

8. VA care is by statute defined to exclude contract care except in specified areas. In providing specific limits on contracting for hospital and medical care, Congress has imposed an exclusive restriction. In other words, the very statutory scheme of chapter 17 supersedes and excludes any application an OMB circular on contracting out might have on the VA as a direct provider of medical care.

9. Title 38 also establishes specific, exclusive policy on contracting in the areas of research and insurance (§ 4101), central administration of house staff stipend and benefits (§ 4114(b)(3)), scarce medical specialist services (§ 4117), staffing of Regional Medical Education Centers (§ 4122), and specialized medical resources (§ 5053). Because the VA is directed or authorized by law to contract in these specific areas, we believe Congress has established a rationale for such contracting different, in most circumstances, from the rationale behind Circular A-76. Under A-76 the intent is that the Government not compete with the private sector and that, in nongovernmental functions, cost-effectiveness must be a criterion for decisions on contracting out. On the other hand, under title 38, the underlying policy is to

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Chief Medical Director (13)

provide a complete and separate medical and hospital service for the care and treatment of veterans. Where conflict arises between A-76 guidelines and specific title 38 mandates or authorities, title 38 must prevail. In other areas where Congress has not been specific, we believe the VA and DM&S must follow the directives of A-76.

10. In your memorandum you specifically pose the question "whether the maintenance and management of DM&S facilities be solely by VA personnel." We believe that Congress intended the management of DM&S facilities and the direct provision of health care, to be a governmental function, but specifically authorized contracting out where deemed necessary to ensure that the VA could meet its mission of providing a complete medical and hospital service. The many specific provisions in title 38 relating to employment preclude any other conclusion. See 38 U.S.C. sections 4103, 4104, 4111, 4114, all relating to employment of personnel to operate the DM&S. See also 38 U.S.C. sections 4105 (qualifications of certain employees); 4106 (exemption of qualifications from Civil Service requirements and a probationary period); 4107 (rates of pay); 4108 (authority of Administrator for personnel administration, hours and conditions of employment, etc.); 4113 (travel expenses of employees); 4115 (authority of Chief Medical Director relating to employment in DM&S).

11. As regards the specific question cited in the above paragraph, however, it is not clear what you may have contemplated in asking whether "the maintenance" in addition to the "management" of DM&S facilities is to be solely by VA personnel. We note that the phrase "management and maintenance" appears, albeit in a somewhat more specific context, in the text of Circular A-76, March 29, 1979. Paragraph 5.f of the circular which defines the term "governmental function" includes among the categories of such functions "[i]n-house core capabilities in the area of research, development, and testing, needed for technical analysis and evaluation and technology base management and maintenance." However, as distinct from the management of the Department and its facilities, as well as the direct provision of medical care, we question whether the "maintenance" of those facilities, if you are referring to routine building and grounds maintenance, for example, can indeed be considered exempt from A-76 coverage.

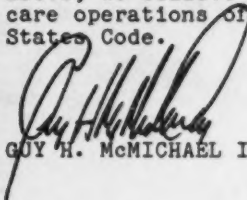
12. We have not attempted in this memorandum to delineate with specificity which areas are or are not covered by OMB Circular A-76. As a general matter, however, we believe that, as distinct from the Department's direct medical care activities and managerial role, support activities (not directly related to patient care and not unique to the

5.

Chief Medical Director (13)

Department) for which VA might contract under section 213 of title 38 would be covered by A-76. For example, we consider general maintenance, grounds care, and laundry service, as among those functions to which A-76 would apply. We will, of course, be pleased to discuss the applicability of A-76 to specific services which might not appear to fall clearly on either side of the line we have attempted to draw.

13. In summary, we believe differing policies are operative in OMB Circular A-76, and in the management of DM&S. The general policy that the Government not compete with the private sector for commercial or industrial products and services underlies A-76. A national policy to provide, as a governmental function, a complete medical and hospital service for our Nation's veterans underlies title 38 and DM&S operations. To apply the rules of A-76 to the basic medical care operations of DM&S, where specific statutes establish the parameters of the mandated governmental function, cannot be justified either legally or on a policy basis. Thus, with the general exception noted above, we believe A-76 does not affect the day-to-day medical care operations of DM&S as delineated in title 38, United States Code.



GUY H. McMICHAEL III

[From the Congressional Record, Vol 127, No. 161, p. S13041—Senate, Nov. 5, 1981]

To the Congress of the United States:

In accordance with the Impoundment Control Act of 1974, I herewith report 72 deferrals of fiscal year 1982 funds totaling \$482.9 million. I am also reporting two new proposals to rescind \$88.2 million in budget authority previously provided by the Congress.

Seventy-one of the deferrals totaling \$391.6 million represent the second in a series of messages that I am transmitting deferring fiscal year 1982 funds made available by the Continuing Resolution, P.L. 97-51.

These actions are being taken in accord with the stated intent of the Congress to provide minimal and temporary funding for the duration of the Continuing Resolution which expires November 20, 1981. As indicated in my last special message of October 20, I plan to restrain spending to insure that the Congress has the opportunity to enact regular appropriations for the entire fiscal year at levels that are consistent with my revised budget request.

Deferrals under the Continuing Resolution are included in this special message for the Executive Office of the President and 20 departments and agencies.

I am also reporting in this message a deferral of \$91.3 million for Veterans Administration construction pending completion of a project review and two rescission proposals for programs in the Department of Defense that are consistent with amendments to the Defense budget sent to the Congress on October 15.

The details of each rescission proposal and referral are contained in the attached reports.

RONALD REAGAN.

THE WHITE HOUSE, October 23, 1981.

[Deferral No. D82-140]

DEFERRAL OF BUDGET AUTHORITY

Agency: Veterans' Administration.

Appropriation title and symbol.

Construction, Major Projects 36X0110¹

OMB identification code: 36-0110-0-1-793.

Grant program: No.

Type of account or fund: No-year.

New budget authority (P.L. 97-51), \$60,844,420.

Other budgetary resources, \$786,528,000.

Total budgetary resources, \$847,372,420.

Amount to be deferred: Entire year, \$91,300,000.

Type of budget authority: Appropriation.

Justification: This account provides funds for the construction and renovation of VA facilities where the project cost exceeds \$2 million. Amounts shown reflect a decision to defer contract awards through FY 1982 for five construction contracts (Chillicothe, Ohio, phased facility replacement; Washington, D.C. nursing home and parking garage; Long Beach, Calif., research and education addition; Palo Alto, Calif. surgical addition; and East Orange, New Jersey, facility renovation). This amount is deferred while the Administration reviews all Major Construction projects for VA medical facilities and considers alternative methods for providing readily available quality medical care for eligible veterans.

Estimated Effects: This deferral action may result in the delay of these projects while VA's medical facility construction program is being evaluated.

Outlay Effect: This deferral action will have the effect of shifting outlays by fiscal year as follows:

1982 into 1983 \$7 million;

1983 into 1984 \$31 million;

1984 into 1985 \$42 million.

¹ This account is the subject of another deferral (D82-141).

Chairman SIMPSON. I would just, I think, say at this point, since it seems that we'll not come again to the opportunity to mention it, that I understand what Senator Cranston is referring to with regard to the deferral of budget authority message here.

But, I don't think that I foresee or perceive any sinister motive there which is going to lead us to mainstreaming. I've read the deferral of budget authority. The amount is deferred while the administration reviews all major construction projects for VA medical facilities and considers alternative methods for providing readily available quality medical care for eligible veterans.

There is, in my mind, nothing sinister about that. What they're going to look into is construction: Whether, for example, we should have a \$276 million veterans hospital near Minneapolis, which is within 5 miles of a facility to be constructed by the University of Minnesota, a multimillion dollar project. We've already protected bed levels, thanks to the assistance of the good Senator from California and others.

I just don't, you know, I wouldn't put the import on that. And if anyone would care to see how the head of the Veterans' Administration feels about mainstreaming, his testimony was very clear at his confirmation hearing. He said that the siren song of mainstreaming and other things were hazardous ideas. He's not going to submit to that. A separate, independent VA system is very important. So, since I won't get an opportunity to do my side of that one, I thought I'd do it at this particular time.

Senator CRANSTON. Fair enough.

Chairman SIMPSON. Thank you.

Senator STAFFORD. I join, Mr. Chairman, in welcoming all of the witnesses here this morning to assist our Senate Committee on Veterans' Affairs, in its consideration of the Veterans' Administration's implementation of Office of Management and Budget Circular A-76. I personally regret I will not be able to stay throughout the morning, because I will be chairing an important markup session of the Committee on Environment and Public Works on Clean Air after I've introduced Governor Snelling of my home State of Vermont at another meeting.

But I will be reviewing the testimony offered. I am especially pleased to greet Dr. Howard Green, the chief of staff of the Vermont Medical Center at White River Junction, and to commend his interest in this hearing in behalf of the National Association of VA Chiefs of Staff.

I also extend greetings to another New Englander who will be testifying, Daniel J. Kearney, from Massachusetts, here in behalf of the National Association of Government Employees. I extend special welcome to Pat Warren of the VA hospital in White River Junction, Vt.

We're delighted all of you could be with us at this hearing.

I think it's very appropriate at this time, for the committee, in its oversight authority, to review what the Veterans' Administration has done, and intends to do, with reference to OMB Circular A-76.

In our review, we must keep clearly in mind the best interests of veterans, and of the taxpayers of the Nation. Circular A-76 establishes the policies and procedures Government agencies are to use

to determine whether needed commercial or industrial-type work should be done by contract with private sources or in-house, using Government facilities and personnel.

Our consideration of contracting-out activities undertaken by the Veterans' Administration should be guided by cost efficiency and cost savings, and also, by the Government's goal of providing employment opportunities for veterans.

Members of this committee have a special responsibility of oversight of the medical care program operated by the the Veterans' Administration. We're interested in providing high-quality medical care for our Nation's sick and disabled veterans. Our responsibility in serving the needs of veterans includes the encouragement of employment of veterans. Our Nation has a good veterans' health care system. That system must be maintained.

Thank you very much, Mr. Chairman.

Chairman SIMPSON. Thank you, Senator Stafford. And I appreciate your attendance.

And Senator Jennings Randolph.

Senator CRANSTON. I'd like to just say, I don't see anything sinister in it, but I am concerned there may be a plan to do something that I think we have to give great consideration to and which I think would be deleterious.

Chairman SIMPSON. I understand. Jennings Randolph, please, sir.

Senator RANDOLPH. Thank you very much, Mr. Chairman, and Senator Cranston, and the members of the committee, who have been here, and who will be able to remain.

The hearing that is chaired by Senator Stafford is a hearing, Mr. Chairman, that I must attend also, as we study the effects of the present Clean Air Act, and the recommendations for perhaps amendments to it. We discuss today the Veterans' Administration's compliance with the Office of Management and Budget Circular A-76. A-76 has to do with contracting to private firms certain Veterans' Administration services.

I am appreciative of the responsiveness, and this is not a pleasantry, of our able chairman, as he arranged and is now chairing this very important hearing.

I think I can, as a member of the committee, speak for 235,000 West Virginia veterans. In our State, we are, concerned of the effect, the possible effect, that the proposed contracting out would have on the Veterans' Administration health-care system. In particular, the services provided by the Veterans' Administration, at centers in Beckley, Clarksburg, Huntington, and Martinsburg. In Martinsburg, we have approximately 1,200 individuals working at the institution.

Mr. Chairman, all Americans share in the responsibility to provide quality health care to those men and women who have served in the Armed Forces, the defense forces, to protect and preserve the freedoms first won over 200 years ago in this country.

I will not support a proposal which will drastically diminish, if that can be shown, the quality health care that the Veterans' Administration medical system presently provides the 30 million veterans who live in this country.

This hearing, I know, shall be a beneficial one. What develops here in the way of testimony will help our Senate staff in the office

of which I am a part, not just the committee, but the offices of Members of the Senate, as we and they study the possible ramifications that this Circular A-76 could have, and may have, on the health care system of the Veterans' Administration.

I shall not be privileged to hear the testimony of Charles Wicks. Charles Wicks has come to the hearing today in a sense, not representing just Martinsburg, but the other three centers that I mentioned in West Virginia. He will discuss the impact that this ruling may have on the employees of the VA centers.

I know that Mr. Wicks' testimony will be helpful. He comes in the capacity of president of the National Association of Government Employees, Local R-478, at the Martinsburg, W. Va. Center.

Again, Mr. Chairman, to you and all members of the committee, this is an important hearing, or the beginning of other hearings, and I shall give attention to the testimony. I shall read it carefully and hope that I may be a part with other members of determining what is practical, the costs that are involved and the results that might result.

Thank you.

Chairman SIMPSON. Thank you very much, Jennings. You, indeed, you've always been a very integral part of this committee's activity.

I recognize Senator Murkowski, please, of Alaska. Do you have any comments?

Senator MURKOWSKI. Thank you, Mr. Chairman. I'll move my breakfast away here, so I can address the Chair.

Chairman SIMPSON. Without objection.

Senator MURKOWSKI. Without objection. Thank you. It's been a policy of the Federal Government, I believe, since 1955, to rely whenever possible on the private sector for goods and services needed to support Government programs.

However, it's been my observation that, while it may be a general policy, it's not necessarily been very closely adhered to.

OMB Circular No. A-76, the focus of this hearing, and I would direct this as a question to the Chair in my opening remarks, my interpretation is that it requires the Government agencies to contract out commercial and industrial work for primarily, if I'm correct, Mr. Chairman, nutritional, janitorial, and mechanical services.

Is that—

Chairman SIMPSON. The contract message—

Senator MURKOWSKI [continuing]. General terms—

Chairman SIMPSON [continuing]. Provides it would be for commercial and industrial-type activities. That is what is referred to as CITA, C-I-T-A instead of C-E, but that's what it refers to. It encompasses about 35,000 VA employees; 21,000 of those will be affected by cost comparison studies to be completed during fiscal year 1982. It does not apply to inherently governmental functions or those where no overriding factors require in-house performance.

Senator MURKOWSKI. Thank you, Mr. Chairman. With your permission, I will proceed, because I think it important to make that identification of the specifics, and as a consequence, oftentimes this type of work can be performed by the private sector at a cost much less than the Federal Government can provide those services for.

We're all aware of the horror stories that exist with regard to Government, the internal bureaucracy associated with ongoing programs that are not examined to make a determination of just what is needed, because there's no relationship, as we know, to the actual cost of those programs, as far as the ability of somebody having to generate a return to support that cost.

And I think the purpose of today's hearing, to explore the effect of this circular on the Veterans' Administration, and the delivery of health care to our Nation's veterans, is certainly in order, and in the best interests of the committee function to look at whether or not the quality can still be maintained but we can reduce some of the redundancy in the system.

I think we are all acutely aware of the continuing need to reduce the cost of Federal Government, to improve our economy, but the realities are, Mr. Chairman, we often talk about it, but we don't do very much about it, and I think this is significant, that we are looking at specifics with the intention of making a determination whether substantial sums can be saved and the quality maintained.

As everyone here is aware, language contained in the conference report requires a specific appropriation to fund cost comparison studies requested by OMB for certain services within the Veterans' Administration.

It's my understanding the estimated cost to complete these studies approached \$30 million and would have come from the Department of Medicine and Surgery budget.

While studies to determine whether or not money can be saved through contracting out at the VA may be necessary, such studies, as I've indicated, need not and should not affect veterans' health-care programs.

If contracting out affected in any degree the current level of patient care provided by the VA, then clearly the savings in dollars would not be worth the cost to the veterans. The Veterans' Administration and the delivery of health care is a fulfillment of an obligation to those of us who have served in our Armed Forces, and the first and last question this committee should ask is whether any new policy could conceivably affect the quality of veterans' services.

I look forward, Mr. Chairman, to the testimony of the many witnesses here today. This is an oversight hearing, the purpose of which is to gather this information. While all questions regarding the appropriateness of contracting out for commercial and industrial services may not be answered today, it is my hope that this hearing will provide the basis for further inquiry.

I thank the chairman and I, too, have to go to the clean air hearing that's going to be starting at 10 o'clock, which has already started.

Thank you, Mr. Chairman.

Chairman SIMPSON. Thank you, Senator Murkowski. Senator Mitchell. And I know you have that other conflict with the clean air hearing, as do I, and I'll be coming down there, with someone taking my place for a few minutes, as I join you. If you would proceed, please.

Senator MITCHELL. I will. There seems to be a remarkable overlap, Mr. Chairman, between these two committees. Many of us

have to get down to that hearing. And I will be joining Senator Murkowski, Senator Stafford, and Senator Randolph.

But I'm pleased that we're going to receive testimony today on proposed contracting-out practices at the Veterans' Administration.

As you know, Mr. Chairman, I expressed concern to you earlier this year about the serious consequences of further implementation of OMB's A-76 directive at the VA facilities. I believe it imperative that this committee thoroughly and fully analyze the potential costs and impacts of contracting out in the VA before any plan is implemented. Everyone here today appreciates the need for continued efforts to achieve efficiency and economy in the Veterans' Administration budget. Veterans, veterans' facilities employees, no less than any other group in our society, recognize the necessity to eliminate unnecessary Government expenditures wherever possible. But there is one overriding concern, that must be the focus of our analysis. What are the effects of these proposals on the quality of medical care provided to our veterans? We must not ever lose sight of that central purpose. The primary responsibility of the VA medical care facilities is to honor the debt that this Nation owes to the men and women who have served their country by providing to them quality medical care and hospital assistance, and we cannot ever allow that goal to be compromised.

Mr. Chairman, as you know, I have serious reservations about the effects of the A-76 directive when applied at hospitals and other health-care facilities. I believe it is our responsibility, which I know you meet and will meet and share, to review the proposed cost study comparisons with careful regard to any potential effect on the quality of health care for veterans.

I look forward to reviewing the testimony of the witnesses here today. I apologize to the first witnesses, that I, as well as the other Senators, have to go to the other hearing, but I will return, Mr. Chairman, as there will be testimony from one gentleman from Maine, Mr. William Rollins, who is the president of the American Federation of Government Employees, Local 2620 at Togus, Maine and Mr. Daniel Kearney, who is the national vice president, First District, of the American Federation of Government Employees. And I want to be back to introduce Mr. Rollins to the committee, and Mr. Kearney, at that time.

I thank you, Mr. Chairman, for your cooperation in this matter.

Chairman SIMPSON. Thank you, Senator Mitchell.

Without objection, I would like to place in the record at this point a statement from Senator Strom Thurmond.

[The prepared statement of Hon. Strom Thurmond, a U.S. Senator from the State of South Carolina, follows:]

PREPARED STATEMENT OF HON. STROM THURMOND, A U.S. SENATOR FROM THE STATE OF
SOUTH CAROLINA

MR. CHAIRMAN:

It is a pleasure to be here this morning to receive testimony concerning the implementation of Office of Management and Budget Circular A-76 and the effects it will have on the present state of medical care provided by the Veterans' Administration to our veterans. This circular establishes the policies and procedures to be used by Federal agencies in determining the economic desirability of contracting out services other than those inherently governmental in nature.

Mr. Chairman, I look forward to the testimony which will be given on this important matter today. For many years I have advocated reduced Federal spending and greater utilization of the vast resources which exist in the private sector of the country. While I want very badly to see that we accomplish these objectives, I feel strongly that we must do so without sacrificing the excellent quality of health care which we now provide to our veterans. We must always place a high priority on repaying the debt that we owe to our veterans and especially to those who were injured in service for this country.

Mr. Chairman, we have a distinguished list of witnesses today. I want to welcome them all and thank them for coming. I want to take this opportunity to extend a special welcome to Mrs. Joan Kershner who is the Director of the Veterans Administration Hospital in Columbia, South Carolina. Mrs. Kershner is a fine lady and is one of the most outstanding directors in the VA hospital system. I look forward to your testimony, Mrs. Kershner, and I hope you will feel free to share with us your personal insights and opinions on this important matter.

Chairman SIMPSON. Well, we do have a large number of witnesses here, and we're very eager to hear their testimony, and we will proceed with the first panel. I again remind you limit to your remarks to no more than 5 minutes, and we will begin with the VA panel, Clyde Cook, Assistant Administrator for Supply Services; accompanied by Dr. Donald Custis, Chief Medical Director; Ms. Marjorie Quandt, Assistant Chief Medical Director for Administration; and Robert Coy, Deputy General Counsel of the Veterans' Administration, Washington.

It's a pleasure to see you all here, and you may proceed, please.

TESTIMONY OF CLYDE C. COOK, ASSISTANT DEPUTY ADMINISTRATOR FOR PROCUREMENT AND SUPPLY, VETERANS' ADMINISTRATION, WASHINGTON, D.C., ACCOMPANIED BY DR. DONALD L. CUSTIS, CHIEF MEDICAL DIRECTOR; MARJORIE QUANDT, ASSISTANT CHIEF MEDICAL DIRECTOR FOR ADMINISTRATION; AND ROBERT E. COY, ESQ., DEPUTY GENERAL COUNSEL

Mr. COOK. Thank you, sir. Mr. Chairman, the requirement of OMB Circular A-76 is that the Government first of all determine which of its functions are governmental in nature and not subject to the circular, and which are not.

Management and control of the agency obviously is a governmental function. In addition, as mentioned by one of the members of the committee, in March 1980, the VA General Counsel provided the legal opinion that based upon the mandates of title 38 of the United States Code, management and direct provision of medical care is a Government function in the Veterans' Administration, and not subject to OMB Circular A-76.

This opinion supports maintaining the integrity of the VA medical care program. This is essential to the mission of the Department of Medicine and Surgery, and to the continuity and accessibility of quality medical care for our veteran beneficiaries. Dr. Custis may have something to say about this later.

The General Counsel's opinion further acknowledged that some functions which support medical care remain subject to Circular A-76. And this legal opinion has been accepted, we understand, by the Office of Management and Budget, as being correct.

However, the question as to what constitutes direct medical care has not altogether been resolved. In March 1979, OMB revised Circular A-76, and issued a comprehensive and complex handbook to make cost comparisons. As a result, the VA inventoried and found that at that time we had commercial industrial activities at 296 of our facilities involving 4,461 activities with over 35,000 full-time equivalent employment, an annual operating cost of about \$700 million, and a capital investment of \$545 million.

Our extensive analysis of this inventory prompted our January 1980 request for a 1-year extension to OMB for a completion of the A-76 review process, and this was granted.

The extension recognized that the activities are as diverse as they are numerous and they include functions performed at our medical centers, our regional offices, our cemeteries and our processing centers.

In May 1980, the agency presented a draft of its proposed implementing directive to the American Federation of Government Employees, the largest union of VA employees. AFGE raised objections to certain aspects of the program, and for some time there was a dialog as to whether or not the directive would be revised.

In April 1981, OMB officials asked that we complete our studies of three particular functions by September 1982. These functions are custodial housekeeping, buildings and grounds maintenance and food preparation and service. They involve approximately 22,800 VA workers. Our deadline for reviewing these activities is September 1982.

There are thousands of activities in the VA for which contracting out could be an alternative. Each of these must be examined under the provision of A-76. Contracting out can be either feasible or it can be expensive. We had some adverse experience in the fifties with contracting out.

Since completing the inventory and analyzing its contents, we have developed an Agency internal directive known as VA Circular 00-81-32, dated July 1981. Our implementing circular establishes an internal management structure for undertaking the reviews and provides specific guidelines with regard to the process itself. In addition, on July 29, 1981 and August 18, 1981, we published review schedules in the Federal Register for the Department of Medicine and Surgery and Department of Veterans' Benefits.

Because of the magnitude of the review program required, it must be decentralized to the maximum degree feasible. Accordingly, heads of field activities were directed to organize management teams to conduct the reviews of the functions to be studied. Because of the importance of the process, the circular provided that each team will be headed by a senior management member of the facility staff, and include other representatives from various specialty areas. The reviews will be accomplished by developing work statements for each individual commercial and industrial activity under review. Prototype statements of work, reflecting these, have been or are being developed in the headquarters at this time. But the prototype statements must be tailored to each service at each facility.

Notice will be placed in the "Commerce Business Daily" of our intent to make these studies, and if two or more responsive firms indicate they are interested, we would proceed with the studies, and obtain firm bids.

At the same time, in-house Government performance cost estimates would be made. The two would then be compared and a determination made as to whether it was more costly to contract out or more costly to continue in-house.

Our directive also specifically names the individuals who would be responsible for reviewing and approving decisions to contract or to continue in-house and provides an appellate process. We have conducted some training for over 550 personnel of our DM&S field facilities on how to perform these studies. We have plans for other training sessions. Because of the nature of DM&S and the size and complexity of the health-care system, DM&S is more susceptible to the application of A-76 than the remainder of the Agency in its entirety.

The cost to the Agency of conducting these studies is somewhat controversial. We have projected an estimate of these costs to be as high as \$29.1 million. But because of the complexity of the review process, it is difficult to come up with a firm, hard estimate. However, we believe that the aggregate cost of full implementation would be quite substantial.

We plan more training in the field. One of the concerns mentioned by the committee was the impact upon veterans' employment. About 64 percent of the work force involved in these functions would be veterans and would have some impact.

Chairman SIMPSON. I must remind you that the time has expired. If you could summarize in just a very few seconds, I'd appreciate it.

Mr. Cook. Just about one more minute, Mr. Chairman.

Chairman SIMPSON. Half.

Mr. Cook. Half a minute. Even though DM&S has begun to implement A-76, that fact alone has caused morale problems. And the impact of Public Law 97-66, of course, has temporarily brought to a halt any further action until clarification is received.

Mr. Chairman, we do contract out for a number of things, equal in value to those activities which we have yet to consider.

Chairman SIMPSON. That's what I wanted to ask, Mr. Cook, if I could. I do appreciate your testimony, and obviously you know the time limitations.

[The prepared statement of Clyde C. Cook, Assistant Deputy Administrator for Procurement and Supply, Veterans' Administration, follows:]

PREPARED STATEMENT OF CLYDE C. COOK, ASSISTANT DEPUTY ADMINISTRATOR FOR PROCUREMENT
AND SUPPLY, VETERANS' ADMINISTRATION

We thank you for the opportunity of appearing before this subcommittee and providing you with information regarding the current status of the Veterans Administration's implementation of Office of Management and Budget Circular A-76. The OMB Circular establishes the policies and procedures Executive agencies are to use to determine whether needed commercial or industrial type work should be done by contract with private sources or provided in-house using government facilities and government personnel.

The circular emphasizes that it is government policy to rely upon the private sector to provide needed goods and services with certain exceptions. Among the exceptions are those functions that are inherently governmental in nature and must be performed by government personnel. Relative costs must also be given appropriate consideration in choosing between in-house performance and reliance upon private commercial sources through contracts. The circular prescribes an analysis of those functions now being performed by federal agencies that are available in the commercial market and are inherently nongovernmental in nature. An analysis need not be performed in connection with inherently governmental functions such as management of government programs, the direction of national defense, conduct of foreign relations, direction of federal employees and regulatory functions of the federal government. If the analysis establishes that savings will accrue from conversion of nongovernmental functions from government workforce to contractor support, the circular directs that the conversion to contract support be accomplished.

The Veterans Administration has examined its various functions to determine

whether or not some or all of them may be inherently governmental in nature. Management and control of the agency obviously is a governmental function. In addition, in March 1980 the General Counsel provided the legal opinion that based upon the clear mandates of Title 38 of the United States Code, management and direct provision of medical care is a government function in the Veterans Administration and is not subject to OMB Circular A-76. This opinion supports maintaining the integrity of the VA medical care program. This is essential to the mission of the Department of Medicine and Surgery and to the continuity and accessibility of quality medical care for our veteran beneficiaries. Dr. Custis may further comment on this important aspect later in the hearing. The General Counsel's opinion further acknowledges that some functions which support medical care remain subject to Circular A-76. This legal opinion has been accepted by the Office of Management and Budget as being correct. However, the question as to what constitutes direct medical care has not been altogether resolved.

The current program began in 1977 when the Office of Management and Budget initiated revisions to the previously existing Circular A-76. At the same time, OMB urged agencies to intensify efforts to complete implementation of the policies that then existed. In compliance, in March 1977 the VA compiled an inventory of functions classified as commercial/industrial as well as identifying the number of employees engaged in performing these functions, their annual operating costs and capital investment involved. This inventory disclosed that there were approximately 3300 activities employing approximately 37,000 persons with an annual operating cost of

\$620,000,000 and capital investment of \$432,000,000. This is one of the largest inventories of commercial/industrial type activities in the Federal government outside the Department of Defense.

Recognizing the magnitude of the program, we began a comprehensive study of what was involved in its implementation. As an initial effort, several studies were made of laundry operations in the Northeast quadrant of the United States and it was determined that either commercial service of the type that was required was not available or that contracting would be more costly than to continue the government operation.

On March 29, 1979, OMB revised Circular A-76 and issued a comprehensive and complex handbook to be used in making cost comparisons. As a result of this reissue, the VA reinventoried and found that at that time, we had commercial/industrial activities at 296 of our facilities involving 4,461 activities with 35,539 full time equivalent employment and an annual operating cost of \$699 million and a capital investment \$545 million. Our extensive analyses of this revised inventory prompted our January 1980 request for a one year extension of the March 1982 deadline for review by agencies of their commercial/industrial activities. This request was based upon concerns that the magnitude of the task required careful planning to avoid disruption of essential agency operations. We were also concerned that the thousands of studies to be conducted would drain our manpower at a time when additional resources are probably not available. OMB subsequently granted the year's extension.

This extension recognized that the activities are as diverse as they are numerous and they include functions performed at our medical centers, at the Veterans Benefits Regional Offices and National Cemeteries and at our Data Processing Centers.

VA Implementation

In May 1980 the draft of the agency's implementing directive was brought to the attention of the American Federation of Government Employees, the largest of the unions of VA employees. AFGE raised objections to certain aspects of the program. The VA allowed a number of months for negotiations to determine the extent to which we could accommodate the union's objection without compromising the agency's responsibilities under the Circular. No agreement had been reached and in May 1981, we concluded that compliance with the OMB deadline would only be possible if we initiated the review of activities covered by the Circular. In April 1981, OMB officials asked that we complete our studies of three particular functions by September 1982. These functions are custodial housekeeping, buildings and grounds maintenance and food preparation and service. They involve approximately 22,800 VA workers. Our deadline for reviewing all other commercial activities in the VA remains September 1983.

The steps taken to date were all preparatory to conducting the actual reviews of activities required to determine whether cost effectiveness would be achieved through contracting out. It is quite clear that there are thousands of activities conducted by the VA for which contracting out could be an alternative. Each of these must be examined under the provisions of Circular A-76. Equally clear is the fact that contracting out can be either feasible or expensive and disruptive. Our past experience in contracting for laundry services in the 1950's proved to be very expensive in the long run due to dramatic escalation in contract prices after the initial contract periods.

Since completing the inventory and analyzing its contents, we have developed a directive within the Veterans Administration implementing Circular A-76. This VA publication is VA Circular 00-81-32, July 31, 1981. Our implementing

circular establishes an internal management structure for undertaking A-76 reviews and provides specific guidelines with regard to the process itself. In addition, on July 29, 1981, and August 18, 1981, we published review schedules for the Department of Medicine and Surgery and the Department of Veterans Benefits in the Federal Register.

Our directive noted that the magnitude of the review program required that it be decentralized to the maximum degree feasible. Accordingly, heads of field activities were directed to organize management teams to conduct the reviews of the functions to be studied. Because of the importance of the review process, the Circular provides that each team will be headed by a senior management member of the facility staff and will include representatives of other specialty areas whose expertise is involved; for example, the activity official, the Personnel, Supply and Engineering Services.

The reviews will be accomplished by developing work statements for each individual commercial/industrial activity under review. These work statements constitute a comprehensive and detailed description of both the quality and quantity of work required to perform a particular function. Prototype statements of work that reflect these factors have been or are being developed for some of our activities. The prototype statements of work must then be tailored to each service at each facility.

Our procedure requires that notice will be placed in the Commerce Business Daily to prospective interested firms to advise them of the activities being considered for review. If two or more responsible firms indicate a willingness to compete for a contract to provide commercial/industrial activity, a solicitation would be developed, issued to known prospective

bidders. At the same time the cost of in-house government performance of the activity will be analyzed. This cost analysis and the commercial firms' bids would be sealed and retained until the specified opening date. On that date, both the government's cost analysis and any bids received would be publicly opened. These would be evaluated. If there are two or more responsible, responsive bidders, their bids would be analyzed and compared with the government cost study to determine the lowest overall cost. The VA Circular specifically names individuals who would be responsible for reviewing and approving decisions to contract or continue in-house activities. An appellate process is also provided.

The cost analysis process specified in Circular A-76 is detailed and most comprehensive. For this reason, we have conducted two major training seminars for over 550 personnel from DM&S field facilities on how to perform these studies. These training sessions focused upon the cost analysis of A-76 and the intricacies of the specified cost procedures. We had plans for other training sessions which would have focused on the various disciplines directly involved in the cost analysis process; for example, the role of personnel in projecting the reduction-in-force related costs and in attempting to minimize employee impact; the contracting officer's role in the bidding process and in contract monitoring and administration; the fiscal officer's role in the provision of cost accounting figures. It is our intention to publish other data and guidelines as we gain more experience in the A-76 process.

Impact of A-76 on DM&S

Because of the nature of the DM&S mission and the size and complexity of the VA health care system, DM&S is more susceptible to the application of OMB Circular A-76 than the remainder of the Agency's departments combined.

Some 3,900 activities in DM&S, affecting perhaps 36,000 employees, were determined to be subject to review under Circular A-76.

The cost to the Agency of conducting the voluminous number of cost-comparison studies in DM&S required by A-76 has been the object of considerable controversy. We have projected an estimate of those costs to be as high as \$29.1 million. The complexity of the DM&S A-76 review makes the development of a reasonably precise cost estimate particularly difficult. However, we believe the aggregate costs of full implementation of A-76 in DM&S would be substantial.

If full, effective implementation of OMB Circular A-76 is to be achieved, the Agency will need to make a further investment. More training of field management staffs will be needed, not only in the procedural and technical aspects, but also in the peculiarities of Federal Reduction-In-Force requirements and techniques, and in methods of managing service contracts. To date, at the national level for example, approximately \$1 million has been expended to train and orient facility management and staff, to develop prototype statements of work, and to otherwise prepare the Agency for implementation.

Aside from direct training needs, substantial indirect training must be accomplished. For example, employees who because of RIF actions shift to prior occupational areas, would often require refresher training.

Other ramifications of A-76 implementation cannot be expressed in dollar terms. For example, the Federal Government leads the way on the preferential employment of veterans, and the Veterans' Administration proudly leads Government in the employment of veterans, especially the disabled. We have found, on a national basis, among some DM&S employees likely to be displaced by A-76 contracts (food service workers; custodial

workers; and plant maintenance workers), sixty-four percent are employed under the Veterans' Preference authorities.

Veterans have greater retention rights than others during Federal employment reductions, and it is difficult to project with any certainty how A-76 contract conversions ultimately would affect their Government employment status. In our larger medical facilities--especially those in metropolitan areas--we expect the impact on Veterans' Preference may be less severe. In rural or isolated areas, and in our smaller facilities, A-76 impact on veteran-employees may be dramatic (this presumes, of course, that contract firms will be interested and qualified to perform DM&S work).

Even though the DM&S has only begun to implement OMB Circular A-76, some impact is already occurring at the facility level. For example, many medical centers have reported employee morale problems--particularly among employees of Building Management, Dietetics, and Engineering Services.

Further cost comparison studies in the Department of Medicine and Surgery have been halted by the recently passed Public Law 97-66. Section 601 of that measure proscribes the use of funds appropriated for medical care, medical and prosthetic research and medical administration and miscellaneous operating expenses for conducting A-76 cost comparison studies. The appropriation request currently before Congress does not contain funds specifically for that purpose. Though some studies could conceivably be funded out of VA's general operating expense appropriation, we believe that the practical effect of this provision of Public Law 97-66 is to prevent the VA from further implementing OMB Circular A-76 in the Department of Medicine and Surgery at this time.

However, there are other commercial/industrial activities in the VA outside the Department of Medicine and Surgery. The inventory of commercial/

industrial activities in these areas lists 532 individual functions affecting 1,806 full time employees. They are distributed among the Department of Veterans Benefits, the Department of Memorial Affairs and to a lesser extent staff offices of the Veterans Administration headquarters. These activities include some functions such as centralized transcription and keypunching, grounds maintenance at cemeteries, gravedigging, automated mailing and some architect-engineering services.

Circular A-76 provides for exemption of some activities under strict guidelines. The VA has exempted some activities in this inventory from further review under A-76. They for the most part reflect the need to maintain a minimal level of in-house capability where short response time is necessary and not available through contract. Exceptions have been granted for such activities as architect-engineering services, certain audiovisual functions at the headquarters and vocational rehabilitation counseling of beneficiaries. Exemptions granted to date have generally reflected concern about disruption of government programs if these services are not immediately available. The impact of a strike or work action by contract employees who are not subject to the same legal prohibitions against striking as government employees has been considered. This threat has not been used as a basis for any of our exemptions. If such actions were to occur, it would be much more critical in some areas than in others.

VA Contracting Record

I would like to emphasize the general policy of the VA in relying upon the private sector. We currently contract for an extensive amount of services. In a procurement budget of a little over \$2 billion, approximately \$700 million is for services which are classified as commercial/industrial.

This \$700 million worth of contracted services approximates the annual operating cost of our current in-house inventory of commercial/industrial activities. For example, in fiscal year 1981 approximately \$9 million was spent for contracts for automated data processing related services; \$72 million for maintenance and repair services including upkeep of roads, walks and grounds; \$15 million for veterans counseling service; \$23 million for the repair of equipment.

An illustration of the mix of in-house and contract services used within the VA can be found in our plant maintenance function. Of the \$622 million expended nationwide in fiscal year 1980 for maintenance and repair operations at our 172 health care facilities, \$292 million was expended through contracts. Of the \$42,100,000 in costs for biomedical engineering, repair and maintenance and inspection, \$20.5 million was for contractual services. Virtually all of the \$130 million expended for nonrecurring maintenance is for contract services. These illustrations are indicative of VA's reliance upon the private sector as specified in OMB Circular A-76. We have a mix of in-house and contract service in many of our functional areas. Generally there has been a trend toward increased reliance upon the private sector for such functions as ambulance service, transportation, refuse and garbage collection, insect and rodent control and plant maintenance and grounds maintenance. We expect this trend to continue, provided it is deemed beneficial from both a management and an economic perspective. We will continue to strive to increase both efficiency and economy of operations. However, as is reflected in Circular A-76, the judgment as to which services are to be performed in house would be based on considerations other than just cost factors, such as the availability of satisfactory service and the relative isolation of many of our facilities with the concomitant nonavailability of prompt service to maintain critical operations.

This concludes my statement, Mr. Chairman. We will be happy to answer any questions that the committee may have.

Chairman SIMPSON. I applaud the breadth of the VA's present contract policy, and I respect the extent to which it is not based on cost factors alone, but could you give me and the committee just a bit more information on the VA's experience with contracting out? What is the total dollar value of the contracts that the VA presently has with the private sector and of that total, what amount now is for commercial and industrial activities?

Mr. Cook. The total value of our contracting out, Mr. Chairman, is something in the neighborhood of \$2 billion. The value of those that we classify as commercial-industrial is approximately \$700 million that we currently contract for.

Chairman SIMPSON. And what is your experience with contracting out? Has it been a good one, a shabby one, where are you with it, in your assessment?

Mr. Cook. Mr. Chairman, we have had experiences ranging from totally unsatisfactory to excellent. It is—you can't generalize.

Chairman SIMPSON. Yes; and I have seen some of the reports on that, and we'll get into that a bit later. But with regard to the limitation on cost comparison studies contained in section 601 of Public Law 97-66, could the VA be required to continue the studies within DM&S by the use of funds taken from other VA budget functions?

Mr. Cook. Mr. Chairman, I'm not sure—I'd like to defer to our Deputy General Counsel to answer that question.

Mr. Coy. Well, the language of the law is very clear that the three specific funds involved could not be used, and employees who are compensated from those funds could not be utilized using at least that type of compensation. I would assume that if in fact there were funds available in other areas, such as general operating expense, you might make some surveys or at least try to begin these types of studies.

Chairman SIMPSON. Mr. Cook, the VA has informally estimated that it would cost approximately \$29.1 million to complete the round of cost comparison studies that is presently due to be completed by the end of fiscal 1982.

What exactly is the basis for that estimate? Do you have anything more than an informal estimate at this time regarding that?

Mr. Cook. Mr. Chairman, we simulated in effect one of the A-76-type studies we would have to make, found that it required approximately three man months, the equivalent of three man months to make the study, and extrapolated that to the number of studies to be made.

Chairman SIMPSON. You indicated that an employee strike of course would be critical in some areas, if that were to occur. What are those areas that would present the most critical disruption of quality?

Mr. Cook. Probably most critical would be food service. Because that must continue.

Chairman SIMPSON. And yet the studies on food service, most of those have a review date in fall of 1982. Is there a reason for that, while the others have a more prompt determination date?

Mr. Cook. That's the largest function we're going to be examining, Mr. Chairman.

Chairman SIMPSON. And are those facilities present in every single VA facility?

Mr. COOK. In every VA health-care facility, yes.

Chairman SIMPSON. And is there contracting out done in those areas of—

Mr. COOK. For food service and preparation, no, sir.

Chairman SIMPSON. Has that ever been considered?

Mr. COOK. Ms. Quandt has something she'd like to respond.

Chairman SIMPSON. Please.

Ms. QUANDT. I would like to respond to the schedule of studies. Food service management is not set aside or later than any other service. That schedule was set so that there would not be grave impact on any one facility by studying all three major services at once. Therefore, they are phased.

Chairman SIMPSON. But they do arrive in the phase-in process in the fall of 1982, with food service. According to my cursory review of—

Ms. QUANDT. Some should be starting in 1982, early in 1982, but proportionately, just as many were, and are, scheduled through the remainder of 1981. For example, by the published schedule, 11 VAMC's were to begin their A-76 cost studies for food service in December 1981. They are Chillicothe, Cincinnati, Cleveland, Dayton, Muskogee, Oklahoma City, Portland, White City, Altoona, and Butler.

Chairman SIMPSON. Did you have anything more you wanted to add?

Ms. QUANDT. No.

Mr. COOK. Mr. Chairman, you asked a question, had we considered in the past. Not in the recent past, but in the past there have been discussions held with those who might provide food preparation service.

However, they were interested in providing the management of the program and not the actual food preparation service, which was not what we were looking for.

Chairman SIMPSON. I see. There are many of those within the country, and highly competitive business in the larger urban sectors.

Let me ask you, Dr. Custis, I think it's more appropriate to direct it to you, since the General Counsel's opinion, which was prepared by Guy McMichael, the one of March 1980, didn't really establish any dividing line between direct medical care functions and support activities, would you care to offer to the committee any meaningful information that would be used to make that important distinction?

Dr. CUSTIS. Mr. Chairman, I've been asked, since the General Counsel opinion defers to the CMD for his definition of direct care personnel, I've previously been asked to give such a definition. I'll be glad to submit that written definition for the record. Referencing it, I believe it can best be defined by exception. The only functions which, in my judgment, can clearly be identified as commercial-industrial, are keypunching, elevator inspection, grounds maintenance, painting, waterproofing, architectural engineering, micro-filming, window washing, meat cutting, and so forth. Personnel involved in these commercial services are in counterdistinction to multi-disciplinary health-care delivery team, which, if quality patient care is to be maintained, include more personnel than just

the physician and the nurse, but also the laboratory technician, the X-ray technician, the radiologist, psychologist; all of those health-care professionals that are essential to an integrated team effort.

I'll furnish this definition for the record.

Chairman SIMPSON. If you would, please.

[Subsequently, the Veterans' Administration submitted the following information:]

OMB Circular Number A-76, "Policies for Acquiring Commercial or Industrial Products and Services Needed by the Government," at paragraph 6(b) allows:

The implementation provisions of this Circular do not apply to government functions as defined in paragraph 5(f). These functions must be performed in-house by Government personnel. (emphasis added)

Paragraph 5(f) of the OMB Circular defines "Governmental function" as "... a function which must be performed in-house due to a special relationship in executing governmental responsibilities . . ." The General Counsel considered these ground rules in his March 21, 1980 opinion to the Chief Medical Director on the applicability of OMB Circular No. A-76 to the functions of the Department of Medicine and Surgery. In the summary paragraph of that opinion, he informed:

... (W)e believe differing policies are operative in OMB Circular A-76, and the management of DM&S. The general policy that the Government not compete with the private sector for commercial or industrial products and services underlies A-76. A national policy to provide, as a governmental function, a complete medical and hospital service for our Nation's veterans underlies Title 38 and DM&S operations. To apply the rules of A-76 to the basic medical care operations of DM&S, where specific statutes establish the parameters of the mandated governmental function, cannot be justified either legally or on a policy basis ... (emphasis added)

It has properly fallen to the Chief Medical Director as the responsible VA official to define the general term "complete medical and hospital service," in order to apply the A-76 policy to the non-governmental, commercial-industrial functions of the

Department of Medicine and Surgery. The Committee requested the Agency furnish, for the record, a definition of "VA direct medical care activities." The Deputy General Counsel advised the Committee this definition is within the sole authority of the Chief Medical Director to determine. By this device, the Chief Medical Director is making such a determination, which follows.

Complete medical and hospital service initiates with management; thus, all medical center and clinic positions classified as executive, managerial, and supervisory, including their administrative support, constitute a governmental function. All the functions and personnel normally aligned under the Patient Care Services component are governmental. These include, in addition to Medicine, Surgery, and Psychiatry, the professional specialties of Neurology, Nuclear Medicine, Laboratory, Radiology, Rehabilitation Medicine, Dentistry, Nursing, Psychology and Chaplaincy. The Allied Health Services are also governmental functions, since they collectively contribute to direct health care delivery, and thus comprise a vital extension of medical care. They are Dietetics (including food service), Pharmacy, Social Work, Library, Voluntary, Audiology and Speech Pathology, Prosthetic and Sensory Aids, and Medical Media Production Services. All personnel working in these enterprises are furnishing a governmental function.

Among the Administrative Services component, Fiscal and Personnel Services provide a governmental function. The former is the principal controller of government funds (including budgeting, accounting, and expending functions) and the latter supports the institution's comprehensive personnel administration program (including representing the government in its labor relations, classifying government employee positions, and administering the government's payroll). These functions contribute directly to the delivery of patient care, since their operations directly concern the resources and staff whose work results in the delivery of care.

The remaining administrative services cannot, in their entirety, be included within the term "complete medical and hospital service." The excluded functions-- those which are commercial-industrial in nature and which must be scrutinized under OMB Circular No. A-76--are identified as follows:

Under Engineering Service,

Plant Maintenance

- Plumbing/Steamfitting
- Carpentry
- Electrical
- Masonry
- Painting
- Air Conditioning/Refrigeration
- Grounds and General Labor

Elevator Inspection

Architect-Engineering, Design, and Drafting

Motor Vehicle Maintenance

Furniture Repair

Under Medical Administration Service,

Reproduction/Duplication

Medical Transcription

Keypunching

Microfilming

Under Building Management Service,

Pest Controlling

Refuse Collection

Window Washing

Carpet Cleaning

Interior Design

Laundry

The functions identified above clearly meet OMB's definition of "commercial-industrial products and services." They are separable from other functions of the Department and are generally available from private enterprise. The Chief Medical Director is, however, ill at ease in including the laundry function among these items for A-76 cost review. VA experience with commercial laundries, as recently as in 1980, makes the Agency very apprehensive over both price and quality of commercial services. Also, the Department is proud of its accomplishments in VA laundry consolidations, which have produced substantial government cost avoidance in recent years. Finally, although one might surmise that laundry service does not substantively impact quality of care, a recent furor over the "cold water wash" initiative vividly demonstrates the continuing concerns of DM&S professional components. In that instance, our overriding worry related to the potential increased incidence of microbial infection related to lowered wash temperature. The cold water wash initiative has been set aside for scientific inquiry on the basis of this professional concern. Nevertheless, a well written statement of work should provide sufficient protection for quality laundry service in the event that conversions to contract are more economical to the government.

Chairman SIMPSON. Mr. Coy, one final question, with regard again to former General Counsel Guy McMichael's opinion, regarding the scope of A-76. He indicated that as a general matter, A-76 should apply only to support activities and not to direct medical care activities or to the VA's managerial role, inasmuch as direct medical care constitutes a governmental function.

And yet in the statutory provision upon which the General Counsel's opinion was based, it provides that the primary function of the Department of Medicine and Surgery "shall be to provide a complete medical and hospital service."

Is it possible for you to reconcile that language with the contracting out of services such as food preparation, that are normally regarded obviously as a very integral and important part of any complete hospital and medical care system?

Mr. Coy. Mr. Chairman, what we were trying to do in this opinion was to indicate that we believe that there was a very unique and important statutory scheme that has been put together over the years that makes it very clear where the responsibility for basic medical care is.

We also tried to avoid what sometimes lawyers try to do, that is to practice medicine. Therefore, we did not define basic medical care. I think that is the prerogative of the Chief Medical Director. He has given his opinion, and I would support what he has just stated. Moreover, I believe it is also consistent with our written opinion. I think that we would make a mistake if we tried to give a lot of examples. That's the Chief Medical Director's prerogative, and I support it.

Chairman SIMPSON. Thank you, Mr. Coy. I have other questions of the panel. I'll submit those in writing.

[The response of the Veterans' Administration to written questions submitted by Hon. Alan K. Simpson, chairman of the Senate Committee on Veterans' Affairs, follows:]

RESPONSE OF THE VETERANS' ADMINISTRATION TO WRITTEN QUESTIONS SUBMITTED BY
HON. ALAN K. SIMPSON, CHAIRMAN OF THE SENATE COMMITTEE ON VETERANS'
AFFAIRS

Question 1: Of the VA's contracts for commercial or industrial activities, what percentage have been terminated before the end of the contract term? (Please break this figure down according to whether the termination was initiated by the VA or the contractor). What percentage ran through the end of the term, but were not then renewed? (Break this figure down according to whether nonrenewal was attributable to another contractor being retained, or to the activity being returned to in-house performance). In the case of all contracts that were either terminated or not renewed, please list the most common reasons for such termination or failure to renew, and please furnish specific information on the total number of contracts entered into, as well as, to the extent practicable, some breakdown of that total according to the reasons for which the contracts were terminated or not renewed.

Answer: The number and dollar value of contracts terminated in FY 1981 prior to completion of the contract term are broken down by the reasons for terminations as follows:

VA Initiated Terminations

<u>Reason</u>	<u>Number</u>	<u>Dollar Value</u>
Service no longer required	14	\$51,819
Converted to in-house	3	\$42,000
Default for non-performance	10	\$258,425
	27	\$352,244
(.5% of all CITA contract dollars)		

Contractor Initiated

<u>Reason</u>	<u>Number</u>	<u>Dollar Value</u>
Insolvency	4	\$318,338
Commercial impossibility	5	\$165,973
Mistake in bid	1	\$30,200
	10	\$514,511
(.734% of all CITA contract dollars)		

The total dollar value of all terminations in FY 1981 amounts to 1.24% of all contract dollars spent for Commercial or Industrial Type Activities (\$700 million).

The number and dollar value of contracts not renewed in FY 1981 are broken down by the reasons as follows:

Contracts Not Renewed

<u>Reason</u>	<u>Number</u>	<u>Dollar Value</u>
Converted to in-house	23	\$263,111
Service no longer needed	12	\$ 34,661
Bids considered too high	7	\$ 35,651
Insufficient Funds	14	\$ 66,628
Determination of non-responsibility	1	\$ 36,000
	57	\$436,051
(.62% of all CITA contract dollars)		

The total dollar value of all contracts not renewed (for any reason other than award to a successor contractor under competitive bidding) in FY 81 amounts to .62% of all awarded CITA contracts.

Our records indicate that 5,963 contracts exceeding \$10,000 were issued in FY 81 covering CITA functions. We estimate that an additional 30,000 contracts were issued which did not exceed \$10,000. Consequently, the total number of contracts terminated or not renewed in FY 81 represents only .3% of all contracts issued in FY 81 for CITA functions.

Question 2: Section 502(a)(2)(C) of Public Law 96-342 requires that DOD contracting estimates of the cost of performance by DOD personnel should be based on an estimate of "the most efficient and cost effective organization" of the function to be contracted out. In conducting the A-76 cost comparison studies, would it be the VA's intention to use this standard, i.e., to study and/or implement such organizational changes, or would your cost estimates be based on current VA performance and organization?

Answer: The VA would make its estimates for use in A-76 cost analyses based on "the most efficient and cost effective organization." The required in-depth review process provides an opportunity for a detailed study of an activity's cost effectiveness. This review can lead to significant savings and more efficient operation. However, because of overall costs of the A-76 review and cost comparison, we believe this ancillary benefit of the process could be achieved by a much less expensive procedure.

Question 3: Paragraph 12 of the General Counsel's opinion says that support activities are subject to contracting out for two reasons: They are not directly related to patient care, and they are not unique to DM&S. Since medical care itself is not unique to DM&S, please explain the relevance of an activity's uniqueness to its classification as a governmental function.

Answer: Within the context of the General Counsel's opinion of March 21, 1981, the term "unique" is used to describe the relation of certain DM&S activities to DM&S's statutorily mandated function of providing "a complete medical and hospital service." Providing such services requires that DM&S conduct a great variety of activities. Many of these activities (maintenance, grounds care, laundry service, etc.) are also conducted in one form or another in other departments of the VA and in most or all other executive agencies. Performance of activities of this type in DM&S does not differ substantially from performance of such activities in any other department or agency. However, many other DM&S activities are unique, particularly within the VA. These are activities which, for the most part, relate directly to the provision of medical and hospital services. Underlying the statutory mandates of title 38, United States Code, is a national policy of providing, as a governmental function, a complete medical and hospital service for our Nation's veterans. These "unique" activities are so directly tied to this governmental function that they cannot be severed from it.

Question 4: Do you see any merit in a limited A-76 test program, or do you feel that A-76 has a sufficient tract record that any test program would be redundant? How and where would you recommend conducting such a study?

Answer: There may be merit in conducting limited A-76 test programs depending upon the function or services being tested. Past experience has provided, as to some functions and services, an adequate basis for evaluating "contracting out." As to these functions and services, test programs would be redundant. We are in the process of considering which other areas, if any, would be appropriate for test programs.

Chairman SIMPSON. And now the ranking minority member of the committee, Senator Cranston, will have an opportunity for questions, and will handle the hearing—

Senator CRANSTON [presiding]. Before you leave, I'd just like to voice a complaint. The OMB didn't get its testimony up to us until 10 minutes before the hearing started today. Normally, it's the OMB that delays other agencies. Today the OMB was quite tardy and didn't comply with our rules. This is not a partisan matter. I've experienced this problem with Democratic and Republican administrations. And if we could call to Mr. Stockman's attention the need to get testimony in time to analyze it, that would be helpful.

Chairman SIMPSON. Indeed, it is not a partisan issue, and I was going to gnaw on the particular representative of the OMB.

That's very tiring to me, and it occurs all the time in the three areas that I chair, this committee, Immigration and Refugee Policy, and Nuclear Regulation, and here's one freshman that's very tired of it. Thank you. I shall return.

Senator CRANSTON. Thank you.

I'd like to start by saying that it seems to me that one of the threshold issues that must be addressed and resolved before the VA begins wide scale activity under Circular A-76 is the extent to which first VA employees have the background and experience necessary to develop adequate and appropriate contract specifications so as to insure that any contracts are for exactly the work that the VA needs done, and that the contracts require the work to be done in a manner that meshes smoothly into the facilities operations. And second, if any contracts are entered into, that VA employees have the ability to manage these contracts.

I believe that both of these functions require very significant levels of skill and experience.

Dr. CUSTIS, does the VA at present, at both the central office and the field station level, have sufficient trained personnel in DM&S and elsewhere to carry out these functions?

Dr. CUSTIS. Senator, I think that the answer to that, in general, is yes. I'm sure the level of that ability varies throughout our facilities. The fact that we currently have 11 percent of our total medical care budget committed to contract-type service shows that we're not without experience in managing contracts.

Senator CRANSTON. Thank you. Mr. Cook, on page 7 of your statement, you note that approximately \$1 million has been expended to train and orient facility management and staff on various Circular A-76 functions.

Isn't that amount really just a drop in the bucket compared to what you will have to spend for adequate training of VA employees to write and manage contracts effectively?

Mr. COOK. It is a minor amount of the total that will be required, yes.

Senator CRANSTON. In the VA testimony, it's noted that the estimated cost of conducting the studies in DM&S that are required in conjunction with Circular A-76 is as high as \$29 million over 2 years.

Don, I know that the Department is experiencing significant fiscal pressure at present because of uncertainty about the fiscal

1982 budget, and concerns that there may be significant cuts this year and in future years.

In fact, I understand that the expansion of the readjustment counseling program, to cite one example in the Department that I have a special interest in, is almost at a stop because of this situation, and that the training for the new Vet Center staff members has been canceled.

As the Chief Medical Director, do you believe that health-care funds should be spent on the Circular A-76 process, when other, very important programmatic efforts in the Department are being cut back?

Dr. CUSTIS. No, sir, I do not, Senator. I would much prefer that funds other than the medical care budget be used, if this is to be done at all.

Senator CRANSTON. I agree with you. Another issue that must be resolved at the outset of any discussion of the relationship between Circular A-76 and DM&S is the reach of the VA's General Counsel's opinion dated March 20, 1980, which I understand OMB has accepted. Bob, I'd like to ask you, in the VA's testimony, it's noted that what constitutes direct medical care has not been altogether resolved.

With reference to the DM&S activities listed in the Federal Register on July 29, 1981, did the Office of the General Counsel analyze and pass on each of these activities as not being part of direct medical care?

Mr. COY. To the best of my knowledge, Senator, we did not.

Senator CRANSTON. Will you do what you can in conjunction with the Chief Medical Director to make such evaluations?

Mr. COY. We'll be happy to, yes, sir.

Senator CRANSTON. On page 1 of your statement, you indicate that the management of Government programs and the direction of Federal employees are inherently Government functions.

Bob Coy, I'd like to ask, in your view, does that mean that the VA, under Circular A-76, could not legally contract for the type of service provided by ServiceMaster Industries, which, in its testimony, describes itself as providing management services to the health-care community, and as managing the hospital's employees?

Mr. COY. I have not read their statement. Circular A-76 certainly, by its own terms, has limitations. It indicates that basic management functions do not come within the purview of the circular. It would appear to me that not only would the legal opinion that we have cited preclude that type of activity, but I think the circular itself probably would. I'd be happy to take another look at it and comment further for the record if necessary.

[Subsequently, the Veterans' Administration submitted the following additional information:]

OMB Circular A-76, by its own terms, is not applicable to the type of management service which ServiceMaster Industries describes itself as providing. Paragraph 6(b) of Circular A-76 states "The implementation provisions of this Circular do not apply to governmental functions. . . . These functions must be performed in-house by Government personnel." Paragraph 5(f) defines a governmental function as "a function which must be performed in-house due to a special relationship in executing governmental responsibilities" and lists several categories of governmental functions. One of the categories is functions which involve "discretionary application of Government authority, as in . . . management of Government programs

requiring value judgments, . . . ; selection of program priorities; direction of Federal employees; . . . Subparagraph 5(f)(1). Clearly basic management of personnel and other Government resources under a contract for management service would require the exercise of such discretionary authority. Thus, such services are not subject to contracting out.

Senator CRANSTON. Mr. Cook, what is the status of the VA's efforts to implement Circular A-76 in the Department of Veterans' Benefits and elsewhere in the agency outside DM&S?

Mr. COOK. Senator Cranston, we have published in the Federal Register our review schedule for the functions in the Department of Veterans' Benefits.

We are within a few days of going to publish the same type schedule for the National Cemetery System. They have been working during this interim on the statements of work, which in effect are the detailed description of what must be done and how well it must be done and how often it must be done, if contracting is to be considered.

Senator CRANSTON. I'd like to have those statements to publish and print in the record of this——

Mr. COOK. Yes, sir, we'll provide them.

[Subsequently, the Veterans' Administration submitted the following information:]

DMA GUIDELINES FOR OMB CIRCULAR A-76 CONTRACTS

MAINTENANCE OF GROUNDS SPECIFICATIONS

This is meant as a guide for National Cemetery Directors and Contracting Officers Representatives (COR).

The local situation will determine which functions will be included in the contract for a particular cemetery. The sample specification and contract "language" for various functions ensure that the contractor knows what services will be required and that proper maintenance is accomplished.

The section on "Contract Administration" covers some of the standard contracting provisions. Other required contract clauses which will be supplied by the Supply Officer at the supporting station.

Copies of contracts, including the cost analysis and the Invitations for Bid, should be furnished to the Department of Memorial Affairs (40D), VACO.

CONTRACTING OF MAINTENANCE FUNCTIONS REQUIRES NOTICE OF COSTCOMPARISON FOR FORMALLY ADVERTISED PROCUREMENTS

Bidders are placed on notice that the solicitation is subject to a Government cost comparison to determine the economic feasibility of accomplishing the specified work in-house or by contract.

The Government's in-house cost estimate will be based on the work statement set forth in the solicitation and shall be submitted to the Contracting Officer in a sealed envelope at least two days prior to the time set for the bid opening. At the time of the bid opening, the lowest evaluated bid price will be determined on the basis of the cost factors cited in the attachment of the solicitation. Attendees will be provided a copy of the cost comparison worksheet for review. Other interested parties will be provided a copy upon request.

A period of at least 15 workdays after bid opening will be allowed for review of the cost comparison worksheet by the interested parties. If the acceptable bid results in an adjusted contract cost lower than the Government's adjusted in-house cost estimate, a contract will be awarded, if otherwise appropriate. If the adjusted in-house cost estimate is lower, the solicitation will be cancelled. All bidders will be notified of the final determination. Copies of the completed cost comparison will be made available upon request.

It should be noted that the Government's cost comparison will be based on a three-year cost estimate. The contractor's bid/offer, if prices for second or third performance have not been requested, and the Government costs (such as personnel) will be straightlined for the second and subsequent years. Only those items of cost for which known changes will occur (includes inflation) will be adjusted for the second and third years. For solicitations involving

firm fixed price type contracts, the second and third year option prices will be used to determine contractor costs for both cost evaluation purposes and for determining firm option prices for subsequent years. This three-year cost comparison methodology is used to average out the typical first-year costs that are normally associated with conversions of one form of manpower to another.

The lowest responsive and responsible bid/offer received will be adjusted to compensate for costs that will be incurred by the Government as a consequence of contracting for supplies and services and would not be reflected in the bid/offer. Examples are:

- a. Transportation costs.
- b. Contract administration and related costs.
- c. Government-furnished materials, supplies, equipment, and facilities.
- d. Incentive or premium costs.
- e. Standby maintenance costs.
- f. Other costs (Severance cost).

The basis for such cost adjustment will be identified.

DESCRIPTIONS - SPECIFICATIONSGENERAL

National Cemeteries are national shrines. The standards of maintenance and appearance of the grounds at these cemeteries must reflect this Nation's concern for those interred therein. Any deterioration in the maintenance and appearance of National Cemeteries would be immediately noted and would adversely affect the VA's mission. For this reason, strict adherence to the specifications is required.

RESPONSIBILITIES

A. The Contractor will supply all labor, material, supplies, tools, and equipment required for the work to be performed under the specifications of this contract.

B. The appropriate Area Director's Office and the contracting office's representative (COR) have line responsibility for contracted cemeteries and will be available to the contractor for consultation and/or questions concerning the work accomplishment. Government may provide if available area for service or for storage purposes. Responsibility for anything stored is the contractor's. The Government is not liable for materials, equipment, etc., that is stored. The term Contracting Officers Representative (COR) means the responsible DMA official designated whether it happens to be a NCAO or NC Director or other government employee is not relevant.

MAINTENANCE TASKSA. Mowing, Trimming and Edging Operations

Contractor will be responsible for mowing, trimming and edging of all grass within the existing developed borders of the cemeteries. Grass will be

cut as necessary to maintain a height of not less than one and one-half (1 1/2") inches nor more than three (3") inches at all times. Concerning lawn mowing height of cut grass will be determined by contracting official representative or cemetery director who will base the decision on climatic conditions and his experience. During the rapid growing season a appropriate effort is necessary to ensure that all grass is properly maintained in accordance with this standard.

Contractor will be responsible for taking necessary precautions to prevent damage to headstones, markers, monuments, flower vases and other structures during maintenance operations. Contractor will provide replacement costs and installation thereof for headstones and/or markers or other cemetery structures or property damaged as a result of actions by contractor personnel.

1. Power mowers, reel or rotary type, will not be operated closer than twelve (12") inches to headstones, monuments, markers, tree trunks or other structures.

2. Grass trimmers, electric or gasoline powered of not more than eighteen (18") inch cutting width, will be used to trim grass from around headstones, monuments, markers, tree trunks or other structures.

3. Riding type lawn mowers, reel or rotary type, may be used. Speed of all lawn mowing equipment will be restricted to that required for safe and prudent operations, but will not, under any circumstances, exceed four (4) miles per hour.

4. No tools or other items will be placed on or leaned against headstones. Contractor personnel will not be permitted to sit or lean against headstones at any time.

5. Cutting blades on mowing and trimming equipment utilized by the contractor must be kept sufficiently sharp so that grass tips are properly cut, not torn or damaged. Cutting heights of all mowing and trimming equipment will be set to prevent any scalping or damage to turf.

6. Accumulations of grass clippings will be removed by contractor within a reasonable time as designated by the contracting officers representative.

7. Grass clippings will immediately be removed from monuments, headstones, monument bases, markers, tree trunks or by other structures by the contractor where accumulation has resulted from maintenance activities.

8. Contractor will edge all sidewalks, curbs, and roadways after each operation or as required by the COR. Cleanup of edging residue will be accomplished after each edging operation.

9. All vegetation will be removed from paved, sidewalk, and curb areas (e.g., cracks or joints in sidewalks, curbs, and roads) under direction of COR.

10. Contractor will coordinate scheduling of all mowing, trimming, edgings and/or other maintenance work to be performed with the assigned cemetery representative to ensure that there will be no conflict with funerals, ceremonies or other ongoing cemeterial functions. Contractor personnel will not operate motorized equipment within two hundred fifty feet (250') of ongoing interment services or other cemeterial activities. The assigned COR will furnish the contractor with a schedule of all interments and/or ceremonies not later than beginning of the cemetery work day. This schedule can be modified at the COR's discretion where a new scheduled interment or activity is necessary.

11. Equipment operation should stop operations during passing of funeral processions to show respect.

B. Refilling Sunken Graves

1. Requirements - Contractor will be required to refill, level and top dress approximately (custom) gravesites yearly. A sunken grave is defined as any portion gravesite that has receded two (2) inches or more from the normal ground level. Refilling sunken graves will normally be accomplished as required. COR will provide the contractor a listing of the areas, grave sections, and numbers of those sunken graves requiring refill. Government will have responsibility for refilling sunken graves for first six (6) months after interment.

2. Procedures - Sunken graves will be filled with regular dirt fill up to the last two (2) inches and mechanically tamped. Topsoil will be applied to normal ground level and new or reusable sod, grass, seed, and fertilizer applied. The area will present a smooth and neat appearance. Sufficient water will be applied to ensure that the area is moistened in accordance with paragraph c below until the COR has accepted the gravesite.

C. Sodding of Gravesites

1. Requirements - Contractor will be required to sod approximately () gravesites yearly. COR will provide contractor with schedule of sod placement and with location of specific sites to be sodded.

2. Procedure - The following procedures will be used to place sod:

a. Area will be raked to receive sod to a depth of not less than two (2) inches. Foreign material greater than one (1) inch in diameter will be removed. The area will be prepared so that when sod is laid it will

be at normal ground level. Soil will be compacted to ensure against sinkage when sod is applied. Soil additives (fertilizer) will be added prior to sodding.

b. Sod will be cut to form around headstones. Sod will be applied smoothly, edge to edge, with staggered joints. The sod will be pressed firmly into contact with the sod bed by tamping or rolling with approved equipment so as to eliminate all air pockets, to provide a truer even surface and to assure knitting without displacement of sod or deformation of surfaces of sodded areas.

c. The area will be adequately watered by the contractor within twelve (12) hours after sodding. Sufficient water will be applied to ensure area is moistened to a depth of not less than four (4) inches. Contractor may utilize any existing water hydrants within the cemetery for watering sod. Contractor will be required to furnish all necessary hose, nozzles, connections, and other equipment required for this purpose.

d. If there are no water hydrants located in the area, contractor will be required to water the area by use of a water truck to perform watering actions. Water trucks will be restricted to paved areas. If the COR determines the contractor must provide water from off-site then cost of water transport will be a contractor expense.

e. If the area does not receive at least one (1) inch of rain within five (5) days after sod is laid, the watering process will be repeated as required by the COR until renovation of gravesite has been accepted.

D. Lawn Maintenance: Seeding

1. Scope - Work consists of seed bed preparation and seeding of

areas of the cemetery where turf has been disturbed or has died for whatever reasons. This includes all newly dug or refilled gravesites.

2. Soil Preparation

a. An area to be seeded or sodded will have a minimum of two (2) inches of topsoil placed on it and be prepared for seeding and/or sodding by bringing ground surface to adjacent grades, (with allowances for sod thickness, where applicable) free of sticks, stones, or other foreign material over one (1) inch in any dimension. Surface to conform to finish grade, free of water retaining depressions, soil friable, free of clumps and of uniformly firm texture. Soil test will be provided for guidance in determination of rate of application of limestone and fertilizer.

b. Ground limestone as specified shall be spread uniformly over designated area if required. Soil test to be made before lime application. Soil tests will be performed by the contractor and results and recommendations given to the COR for full compliance. Contracting Officer will be given a copy for his file.

c. Fertilizer - Perfolizer shall be spread with approved equipment and at an even rate determined by COR over the area to be seeded.

d. Work limestone and fertilizer into entire depth of topsoil and grade to smooth surface ready for seeding/sodding. At no time will hydrated lime and fertilizer be applied together.

3. Seeding

a. All areas to be seeded at rate recommended by the COR.

b. Seed shall be uniformly distributed by hand, broadcast drill, or cyclone spreader or other approved method. Seed will be roller into the soil immediately after spreading.

c. Seeding shall take place under the director of the COR. Approval of the Director will be required before seeding is to begin. No seeding to be done during windy weather or when ground is wet or otherwise un-tillable.

d. Mulching.

1) All seeded areas shall be mulched as required by COR immediately following seeding. Chopped straw to be evenly applied at a uniform rate so as to provide a loose depth of covering thin enough to expose a small portion of soil yet reduce washing to seed and soil, 1 bale per 1,000 sq. feet of straw.

2) Contractor is responsible for any disfigurement or damage to structure or property on or adjacent to the area, and is responsible for replacing mulch if required.

E. Removal of Leaves

1. Requirements - Contractor will be required to remove all fallen leaves from the cemetery grounds as determined by the COR.

2. Procedures -

a. Leaves will be raked, vacuumed, or blown into windrows adjacent to the curb. Leaves will then be picked up and removed from cemetery grounds by the contractor immediately. The contractor will provide a suitable disposal area after removal from the cemetery.

b. COR will inspect all areas of the cemetery during this period to ensure that there will be no undue accumulation of leaves in any area. COR will advise contractor to schedule removal work accordingly.

3. Grounds Cleanup - Any turf or structure damage incurred in leaf removal process will be repaired at contract expense under the COR's direction.

a. Contractor will be responsible for removal of all trash, debris, dead or unsightly flowers and fallen tree limbs or branches in all cemetery areas.

b. Contractor will be responsible for removal of unsightly floral arrangements left on gravesites after interment. These items will be removed in accordance with posted floral regulations.

c. Contractor will provide for removal of these accumulated materials from the cemetery and provide for a suitable disposal area.

d. Contractor will be notified by COR of any areas or gravesites where flowers are not to be removed. Approximately () gravesites per month will require cleaning.

e. Contractor will provide sufficient laborers, as determined by the COR, each workday for pick up and removal of materials and will provide a suitable conveyancy for movement on cemetery grounds.

f. Contractor will provide emergency pickup at the COR's discretion within six (6) hours of notification.

F. Raising and Realigning Headstones:

1. Headstones are set at each individual grave on the centerline.

They must be plumbed and aligned laterally, transversely and diagonally with headstones at other graves. When realignment is scheduled, the older type markers should be set as follows:

- a. Upright type - 35" inches x 10" inches x 2" inches - set 18" inches out of ground.
- b. Unknown type - 30" inches x 6" inches x 6" inches - set 12" inches out of ground.
- c. In the newer sections all upright headstones will be set at a nominal height of 24" inches from the finished grade to the top of the arc. There headstones have been previously set at other heights above grade, but in general at a uniform height throughout an area and otherwise present, a neat overall appearance with the inscription visible, resetting for the sole purpose of attaining the stated heights will not be required. The nominal height of 24" inches given for the current standard of headstone setting is the average height. Minor deviations in less than the nominal height are permissible to provide a fair and pleasing top line and to compensate for slight ground rises or depressions within a burial section. Where a considerable number of adjacent stones are set or reset in a section and ground conditions are known to require an allowance for vertical settlement an extra 1" inch may be permissible in the above ground projection when the stone is initially set. There are approximately () headstones/markers. Flat markers will also be realigned in accordance with COR's directions to keep the face no more 1" inch above and parallel to the ground.
- d. Where the standard flat marker is used, it will be set on the gravesite with its top edge 7" inches from the head of the gravesite and

centered on the width of a grave. The face of the marker will be set 1" inch above and parallel to the surface of the ground.

G. Headstone Cleaning:

1. Headstones and markers will be cleaned to remove objectionable accumulations, such as bird droppings, mud, tire or hose markings, grass, grass stains, residue from trees, fungus and so forth. The toning or patina of the stone will not be removed unless as a result of cleaning accomplished to remove the accumulations previously noted. In this instance, the stone should be cleaned in its entirety so as to present a uniform appearance. The method of cleaning will be subject to approval of COR.

2. All Government headstones and markers will be cleaned once a year prior to Memorial Day or as often as deemed necessary to assure clean appearance. Caution will be used to assure that the compound does not harm the turfed areas. There are approximately () headstones requiring cleaning.

H. Fertilizing, Seeding, and other Lawn Care

1. Scope:

Contractor will be responsible for maintaining the turf area of the cemetery in a healthy condition by proper application of fertilizers, chemicals (to control weeds, diseases, and insect pests) and lime (if soil test indicates it is needed). Aeration will be accomplished _____ times per year on dates determined by the COR. /pproximately _____ acres will require aeration each year.

2. Equipment and Supplies:

a. Contractor will supply all necessary applicators, hoses, and other equipment.

b. Water will be furnished by the Government at no cost to the contractor.

c. The Government will furnish all materials and supplies required by the contract.

3. Procedure:

a. Contractor will be responsible for taking all precautions to prevent damage to headstones, markers, monuments, flower bases, trees and other structures during maintenance operations. Contractor will be charged current replacement costs for headstones/markers or other cemetery structures or property damaged as a result of actions by contractor personnel.

b. Contractor will conduct _____ soil tests at locations designated by COR and will provide COR test results on a timely basis.

c. Fertilizer - Shall be applied according to the soil test conducted by contractor for each section tested. The formulation of nutrients shall be based on soil test. Application dates will be set by COR.

d. Lime - If soil tests indicate a need for lime, it shall be applied at the rate indicated by those tests. Time of application shall be late fall or early winter unless local practice indicates another time of year to be more favorable. Determination of rate and date of application shall be made in writing by the COR.

e. Seed provided to contractor by the government will be spread _____ times per year at times determined by COR.

f. Weed and Disease Control - All weed growth and disease shall be controlled by means of spray or other methods as approved by the

Director. All personnel using such sprays shall be licensed by the appropriate State/Commonwealth of _____ to use pesticides.

g. Insect and Rodent Control - Will be by means of gas, traps, or other methods approved by COR as required by State or Federal Regulations. Soil shall be tamped into holes and turf replaced or reseeded (by licensed individual or company) to incure acceptable appearance.

4. Soil Preparation:

a. An area to be seeded or sodded will have a minimum of two (2) inches of topsoil placed on it and be prepared for seeding and/or sodding by bringing ground surface to adjacent grades, (with allowances for sod thickness, where applicable) free of sticks, stones, or other foreign material over one (1) inch in any dimension. Surface will conform to finish grade, be free of water retaining depressions, with soil friable, free of clumps and of uniformly firm texture. Soil test data will provide COR guidance in determining rate of application of soil additives.

b. Ground limestone shall be spread uniformly over designated area if required. Rate shall be determined by soil test. Soil test to be made before lime application. Soil tests will be performed by the contractor and results and recommendations given to the COR. Contracting Officer to be given a copy for h/s file on a timely basis.

c. Fertilizer will be spread with approved equipment and at a rate determined by the COR over the area to be seeded.

d. Limestone and fertilizer will be worked into entire depth of topsoil and graded to a smooth surface ready for seeding/sodding. At no time will hydrated lime and fertilizer be applied together.

5. Seeding:

a. All areas will be seeded at rate recommended by the COR.

b. Seed shall be uniformly distributed by hand, broadcast drill, or cyclone spreader or other approved method. Seed will be rolled into the soil immediately after spreading. Seeding will take place at the discretion of the COR.

c. Mulching.

1) All seeded areas will be mulched as required by the COR immediately following seeding. Chopped straw to be evenly applied at a uniform rate so as to provide a loose depth of covering thin enough to expose a small portion of soil yet reduce washing to seed and soil, 1 bale per 1,000 sq. feet of straw.

2) Contractor is responsible for any disfigurement or damage to structure or property on or adjacent to the area, and is responsible for replacing mulch if required.

6. Sodding:

a. Description - This item consists of furnishing, hauling and placing grass sod on areas and gravesites as specified herein. The COR will provide the contractor with location of specific sites to be sodded.

b. Materials - Cultivated Grass Sod - All grass sod to be certified and obtained from State Certified nurseries and have been grown on natural native mineral soils comparable to those afforded at job site. Grower's name, together with substantiating information as to field location from which sod is to be cut and species, percent purity and/or mixture of grass sod to be

applied to be submitted for Director's approval prior to delivery. Failure to obtain advance approval will constitute grounds for rejection of all sod delivered to site. (Invoices for all sod will clearly state point of origin have and attached to them a facsimile of Grower's Nursery Certificate issued by Department of Agriculture or a certified delivery ticket per truck load). All grass sod will meet the following basic requirements:

- 1) Sod free of disease and soil borne insects.
- 2) Sod free of clover, broadleaf and/or other noxious weeds. (Sod considered free of such weeds if less than two (2) such plants are found per 100 square feet of area.)

- 3) Sod of uniform color and density and contain:

VARIETY OF SOD

% OF VARIETY

or approval equal.

- 4) Sod will have been mowed to the proper height prior to stripping and have been maintained for a minimum of three (3) months at or near height or final clipping at nursery.

- 5) Sod relatively free of thatch. Thatch build up which significantly detracts from appearance of sod may be sufficient cause for rejection.

6) Sod machine stripped at uniform soil thickness of approximately 3/4 inch. (Measurement for thickness to exclude top growth and thatch.)

7) Individual pieces of sod will be cut to supplier's standard width and length. (Maximum allowable deviation from standard widths and lengths 5%.) Broken pads, torn or uneven ends are not permitted.

8) Root development to be such that standard six foot pieces will support their own weight and retain their size and shape when suspended vertically from a firm grasp on uppermost 10% of the area.

9) Under moderate moisture conditions, weight to not exceed 7 pounds per square foot - minimum weight not less than 4 pounds per square foot.

c. Construction Methods:

1) All sod will be transplanted within 24 hours from the time it is harvested. All sod in stacks will be kept moist and protected from exposure to air, sun, and freezing. Any sod permitted to dry out will be rejected, and no payment made for rejected sod.

2) Before placing or depositing sod upon any surfaces, all shaping and dressing of such surfaces as described under SOIL PREPARATION will be completed. Area will be watered lightly before the placing of sod; sod will not be placed on dry surface. Completed areas will be sodded to be smooth, uniform, well-tilled surface true to line and cross-section, and any raking accomplished at no additional cost.

3) No sod will be replaced at any time temperature is below thirty-two (32) degrees Fahrenheit. No frozen sod to be used and no sod to be placed upon frozen, dry or excessively wet soil.

4) Sod will be lifted from trucks or storage piles by hand and placed with closed joints and no overlapping. All cracks to be closed with small pieces of sod. After laying sod will be watered thoroughly and then tamped. "Tamping" consist of firmly closing seams between strips by use of hand tampers or approved rollers. Any slipping of sod will be corrected. Sod laid on excessive slopes shall be pegged.

5) Adequate and watering equipment must be on hand before sodding begins, and sod will be kept moist until root system adheres to original seed bed and becomes established and accepted by the COR.

6) Sod shall be laid with long edges parallel to contours, except in swale or pitch where it shall be placed perpendicular to flow line. Successive strips will be neatly matched and all joints staggered. Sod will be laid in all areas indicated on plan provided by COR.

7. Guarantee: The Contractor shall be responsible for mowing and watering sodded and seeded areas and maintaining them in a healthy, vigorous condition until all contracted work is completed and accepted by COR.

Mowing, will be often enough so that no more than 1/3 of leafage is removed at any one mowing.

The contractor will at his own expense, replace any seed or sod which has died or been damaged during the establishment period (consists of three (3) grass cuttings).

I. Plant Material Maintenance

1. Scope:

Work consists of maintaining shrubs and trees in a healthy, attractive condition by proper fertilizing, pruning, spraying for pests, cultivation, and mulching.

2. General Requirements:

Personnel will be properly trained in the operations they are to perform. If pesticide sprays are used the person in direct charge will be licensed by the appropriate State/Commonwealth.

3. Equipment:

- a. All necessary equipment will be furnished by the contractor.
- b. All cutting tools will be kept sharp and properly functioning.
- c. Materials for spraying, fertilizing and mulching will be supplied by the government. The government will furnish all required chemicals, fertilizers and other supplies. The COR will furnish the necessary formulation of fertilizer and the required amount of lime as determined by the soil tests.

4. Procedure:

- a. Trees will be kept free of suckers and broken branches.
- b. All cuts will be made cleanly and properly dressed.
- c. The saucers (watering basins) around young trees will be kept free of grass and weeds. Shredded pine or fir bark mulch (or equivalent) will be added when required. No bark chips or nuggets will be allowed.

d. Any tree showing adverse affect from high wind will also be staked. Trees which have been damaged in any way will be reported to the Director, or his authorized representative, then properly treated to insure a proper healing of the damage. All plant material destroyed by the contractor will be replaced at his cost.

e. Hedges and shrubs will be trimmed to promote healthy, attractive appearance and uniform growth over all parts of the plant with the bottom wider than the top. Hedges and shrubs shall be kept neat in appearance and free of dead branches and leaves. Clippings will be removed by the contractor.

f. Beds containing shrubs, groundcover and annual or perennial flowers shall be kept attractive and free of weeds. Any cultivation shall be shallow to avoid any damage to roots. Pre-emergent herbicides may be used if compatible with the plants in the beds and if authorized by the COR. Dead or dying material shall be reported to the COR. Replacement plants, if needed, will be furnished by the government and planted by the contractor.

5. Fertilizing:

Dry fertilizing of established trees.

a. Formula: Supplied by the Government.

b. Methods: Punch-hole with power-driven or hand bar. Drilled-hole with power-driven or hand auger. Aero-Fertil method. When holes are drilled, the soil brought to the surface by the auger should be thoroughly removed from fine turf when the job is completed.

c. Location of Holes: Start holes 2 1/2' or more from base of trunk. Keep far enough away to prevent injury to base of the trunk or root

flange. Stagger holes about 2' apart and locate them in circular patterns underneath the crown-spread to the outer tips of the branches.

d. Depth of Holes: 10 to 15 inches.

e. Amount of Fertilizer per Tree: 3 - 5 pounds for each inch of trunk diameter measured 4 1/2' above ground. In determining the amount of fertilizer to use per tree, consider the soil area in which fertilizer can be applied. If the area beneath spread of the branches is restricted, reduce the application in proportion to the number of holes that cannot be made. Trees growing between the sidewalk and a paved street should rarely received over one-half the amount of fertilizer indicated by measuring the trunk diameter at 4 1/2' above ground.

f. Method of Application: Start inside, near the trunk, and work out toward the drip of the branches until the prescribed amount of fertilizer is used. Trees with spreading root systems, such as elm and maples growing in clay soil, often will have roots beyond the dip of the branches. In such cases it is well to extend the area fertilized, especially if all of the fertilizer has not been used under the branch spread.

g. Filling of Holes: Place one cup of fertilizer in each hole. Finish filling holes with humus, Michigan peat or soil. If soil is heavy clay, the holes may be left open or filled with sand to improve aeration and to enable water to penetrate more readily.

Closing of Holes: If desirable, in sodded areas, the holes may be closed by pressing from different angles with the heel of the worker's shoe.

Aero-Fertil Method: This is a good method of aerating the soil and distributing fertilizer, especially in case of trees growing in heavy soil. Holes are drilled in much the same pattern as described previously except that they are usually placed 3 - 4' apart and 15 - 18" deep. by use of a special piece of equipment (Aero-Fertil Gun) a charge of compressed air from a compressor is injected into the drilled hole. This blast of air fractures the soil for some distance from the point of entry. Fertilizer, and humus, if desired, is then blown into the hole and through the fractures in the soil by a second blast of air.

h. Fertilizing of trees is performed in the dormant periods one time per year on dates to be determined by the COR.

6. Liquid Fertilizing of Established Trees

a. This method may be substituted for dry fertilizing with the COR/Director's approval.

b. Formula: Soluble fertilizers are available on the market with analyses, such as 15-15-15, 20-20-20, 24-12-12 and others. Brand names of some soluble fertilizers used for feeding trees are Heller-Gro, Fermal, Millers, Ra-Pid-Gro, Kapco.

These materials are used at dilutions of 2 - 10 pounds per 100 gallons of water and 5 - 7 gallons of solution is used per inch of trunk diameter of the tree being fertilized. With any brand of soluble fertilizer used in liquid feeding, the directions given by the manufactures should be followed.

c. How Applied: Use hydraulic sprayer at 200 lbs. pressure and a soil spear with shut-off valve.

d. Distance Between Injection Points: 2 1/2 - 3'.

e. Area to be Covered: Start near the trunk and work out to the drip of the branches. In clay soil it is well to go beyond the branch tips.

f. Times Per Year: Twice, if needed - late spring and midsummer.

7. Fertilization Guidelines

a. In determining the amount of fertilizer to be used on trees that stand in close groups, consideration must be given to overlapping root areas.

b. For fertilizing American Beech and Crab Apples, reduce applications of inorganic fertilizer to one-half the amounts suggested by dry or wet methods.

c. Use care not to over-fertilize small trees. A little extra fertilizer for small trees can result in an overdosage, which can be fatal to the plant.

d. Don't fertilize trees growing in heavy soil when the soil is excessively wet.

e. Keep the basic fertilizer at least 2 1/2" below the top of the hole in turf areas to prevent burning of the grass by dehydration. Watering after applying fertilizer will help prevent injury to turf.

f. In fertilizing trees that contain shrub beds within the root area of the tree, care must be taken not to punch holes closer than 6" to

the crowns of small plants. Azaleas, andromedas and other small plants will die from fertilizer in holes placed too close to the plants.

g. Liquid feeding when heavy soils are excessively wet will further exclude the soil air and may be detrimental to the tree. Liquid feeding is most beneficial when the soil is on the dry side.

h. When trees are transplanted to compacted soils the Aero-Fertil equipment is an excellent method of fracturing the soil and distributing fertilizer beyond the original planting hole.

i. Large evergreen trees can be treated the same as deciduous trees with respect to fertilizing.

10. Fertilizing Shrubbery

a. Fertilizer composition should be same as for trees.

b. Amount: Apply one cup of fertilizer per every two feet of spread of the plant. The fertilizer should not be closer than one foot from base of shrub and extend to the perimeter of the branches.

c. Method: Fertilizer should be applied by sprinkling onto the surface of the soil.

J. Pruning Standards for Shade Trees

1. Scope:

Work consists of pruning of dead, dying, diseased, interfering, objectionable and weak branches.

2. General Requirements:

There are four (4) types of classifications of pruning. Class 1 -

fine pruning, Class 2 - medium pruning, Class 3 - safety pruning, Class 4 - cut back or topping. Any debris resulting from pruning will be removed by contractor.

3. Procedure:

a. Class 1&2 - Fine/Medium Pruning

Removal of dead, dying, diseased, interfering, objectionable, and weak branches.

Fine pruning shall consist of the removal of the described branches on the main trunks and limbs inside the leaf area and any that extend beyond this area. The described branches to 1" diameter may remain within the main leaf area to their full length.

This work must be accomplished with the following specifications:

- 1) All cuts to be made sufficiently close to the parent stem so that healing can readily start under normal conditions.
- 2) All limbs one (1) inch in diameter or over must be precut to prevent splitting. All branches 3 1/2" and over in diameter should be lowered by proper ropes to the ground.
- 3) Remove one of all crossed or rubbing branches where practicable so the removal will not leave large holes in general outline of the tree.
- 4) On trees known to be diseased, tools are to be disinfected with alcohol after each cut and between trees, where there is known to be danger of transmitting the disease on tools.

5) Old scars not healing properly and where callus growth is not already established are to be traced and treated.

6) All girdling root visible to the eye, where practicable, should be treated as follows:

- a) Cutting of root at either end.
- b) Notching of root in center with chisel.
- c) Removal of entire root without injury to bark or parent stem.
- d) Report girdling roots.

7) Any structural weakness, decayed trunk or branches, split crotches, or branches, will be reported to the director.

b. Class 3 - Safety Pruning

Removal of dead, diseased or weak branches.

Safety pruning shall consist of the removal of the described branches to a size that in falling would injure a person.

This work is subject to the following specifications:

- 1) All cuts to be made sufficiently close to the parent stem so that healing can readily start under normal conditions.
- 2) All limbs over two (2) inches in diameter to be removed by precutting to prevent splitting. Lowering of any branches by proper ropes that would injure the tree by falling.
- 3) On trees known to be diseased, tools are to be disinfected after each cut and between trees with alcohol, where there is known to be danger to transmitting the disease on tools.

4) Any structural weakness, decayed trunk or branches, split crotches, or branches, should be reported to COR on timely basis.

5) Suggested minimum for safety pruning . . . remove limbs to two and one half (2 1/2) inches diameter and five (5) feet in length. Account should be taken of location of tree and tree variety in applying the above.

c. Class 4 - Cut Back or Topping

The reduction of tops, sides, underbranches or individual limbs.

This work must be accomplished with the following specifications:

1) All cuts to be made sufficiently close to the parent stem so that healing can readily start under normal conditions.

2) All limbs one (1) inch in diameter or over must be precut to prevent splitting. All branches 3 1/2" and over in diameter should be lowered by proper ropes to the ground.

3) On trees known to be diseased, tools are to be disinfected with alcohol after each cut and between trees, where there is known to be danger of transmitting the disease on tools.

4) Old scars not healing properly and where callus growth is not already established are to be traced and treated.

5) All girdling roots visible to the eye, where practicable, should be treated as follows:

- a) Cutting of root at either end.
- b) Notching of root in center with chisel.
- c) Removal of entire root without injury to bark or

parent stem.

- d) Report girdling roots.

6) Any structural weakness, decayed trunk or branches, split crotches, or branches, should be reported.

4. Methods:

a. When cutting back or topping trees, drop crotch as much as possible, avoid cutting back to small suckers. Remove smaller limbs and twigs in such a manner as to leave the foliage pattern evenly distributed.

b. In reducing overall size, attention is to be given to symmetrical appearance. Top is to be higher and sides reduced in order to maintain a tree-like form.

c. On thin bark trees, just enough limbs should be removed to get the effect wanted without admitting too much sunlight to the trunk of the tree or to the top of the large branches. Care should be taken with the following trees: Lindens, Sugar Maples, Red Maples, Beaches, Apple, Oaks and other trees susceptible to sunscald growing in different geographical areas. The above damage may be minimized by doing work on susceptible trees during the dormant season.

d. When cutting back trees, one should have in mind to make them shapely and typical of their species.

e. In lifting the bottom branches of trees for underclearance, care should be given to symmetrical appearance, and cuts should not be made so large they will prevent normal sap flow.

f. Periodical cut back or topping of Silver Maples, Poplars and other trees with brittle and soft wood is an established practice and has proven beneficial in maintaining the safety of these trees over long periods of growth. Other trees with soft and brittle wood growing in different geographical areas may be specifically named when it is common practice to control the growth by cut back or topping.

g. In general reduction of size (cut back or topping) not more than one-third of the total area should be reduced at a single operation.

K. Trash, Tree, and Debris Removal

1. General:

All work under this section is subject to the General Requirements to Bidder which form a part of these specifications, and the contractor shall be responsible for and governed by all the requirements thereunder.

2. Scope:

Work consists of collecting and removing all trash, trees, debris, dead or unsightly flowers, tree limbs, as well as any other debris within area defined by COR, in accordance with the floral regulations of the cemetery.

3. Requirements:

a. All trash, debris, contents of trash cans, dead or unsightly flowers and fallen tree limbs will be removed from the cemetery areas a minimum

of once every other day during the week and year around.

- b. All grave decorations will be removed twice a month.

Approximately _____ graves a month will require this maintenance.

- c. Contractor will provide necessary labor and suitable conveyance each work day for pickup of this debris from cemetery grounds.

- d. Removal of debris and disposal off the cemetery grounds will be the responsibility of the contractor. The Contractor may not use trash bins provided for the cemetery under a current solid waste disposal contract.

OTHER CONTRACT PROVISIONS

A. Standards of Contractor Employee Conduct and Safety - Contractor and contractor personnel will be required to adhere to the following standards of dress, safety practice, and behavior while performing work in the national cemetery:

1. Be fully clothed in uniform clothing at all times, including an upper garment to cover the body from waist to neck. The uniform will include sleeved shirt, full length trousers, matching jacket, if needed. The company name shall be sewn over the left pocket of all shirts and jackets.
2. All clothing and safety equipment will be provided by contractor.
3. Steel toed shoes will be worn at all times. Other safety equipment (i.e. hard hats, safety glasses) will be worn as prescribed in national cemetery regulations.
4. Refrain from loud or boisterous behavior or use of profane or abusive language.

5. Employees will not sit, lean or stand on any headstone/marker.

6. Employees will not place or lean any tools or other articles on any headstone/marker.

7. Employees will not eat or drink beverages except water while in work areas. Use of intoxicating beverages and/or drugs is prohibited.

B. Use of Cemetery Facilities

1. The contractor will provide his own restroom, lunch, storage, and other areas. The government may lease unused facilities to the contractor. The government will not be responsible for any loss, damage, or theft of items in the contractor's area nor will phone services be provided. The contractor will be responsible for acceptable standards of housekeeping and custodial maintenance.

2. Contractor employees may park privately-owned vehicles in the area designated by the cemetery representative for employee parking.

3. Contractor will not operate trucks, tractors or other heavy equipment on any turf except as designated by the COR and/or director.

C. Supervision and Training

1. Contractor will provide an employee supervisor on the cemetery grounds at all times that contractor employees are performing work. Contractor will be responsible for maintaining satisfactory standards of personnel conduct and work performance and will administer disciplinary action as required. Contractor shall remove employees for cause, to include, but not limited to, misconduct in performance of duty under their specifications and conduct contrary to the best interests of the Government. Contractor shall rely on

the judgement of the COR in making such determinations.

2. Contractor will be responsible for proper training and safety of contractor employees performing work under these specifications. OSHA standards will be observed by the contractor in all work performed. Appropriate safety equipment will be furnished by the contractor to contractor personnel and will be used as prescribed by OSHA standards.

3. COR reserves the right to direct contractor employees for non-scheduled work (i.e. cave ins, correcting complaints) up to a maximum of _____ hours per week.

D. Contract Administration

1. Contract Period and Performance - *Contract period will be one year from (Oct. 1, 1981) to (September 30, 1981). All contract services will be performed at the National Cemetery. The apparent low, responsive, responsible bidder will be required to submit evidence of experience in similar types of ground maintenance operations.

2. Inspection and Acceptance - The COR will be designated, in writing, at the time of the award of the contract. The COR will be the Cemetery Director, Assistant Director, or other Government employee as designated by the Director, National Cemetery Area Office. Inspection and acceptance of contract services is the responsibility of the Contracting Officer's representative. Government personnel performing inspection of contract services are not authorized to issue orders or direct the work of contractor. will provide necessary operational information through the contractor or the chief supervisor of the contractor personnel.

3. Option to Extend the Term of the Contract - This contract is renewable, at the option of the Government, by the Contracting Officer giving written notice of renewal to the Contractor at least sixty (60) days before the contract is to expire. Such a preliminary notice will not be deemed to commit the Government to renewals. If the Government exercises this option for renewal, the contract as renewed shall be deemed to include the option provision. However, the total duration of this contract, including the exercise of any options under this clause, shall not exceed three years.

4. Option to Extend Services - The Government may require the contractor to continue to perform any or all items of services under this contract within the limits stated. The Contracting Officer may exercise this option, at any given time within the period specified, by giving written notice to the contractor. The rates set forth shall apply to any extension made pursuant to this option provision unless provision for appropriate price adjustment has been made elsewhere in the contract.

All prior items are subject to option clause. Department of Labor wage rate changes shall subject the contract to price adjustment by negotiation if a cost increase results to the contractor for the option period. The Government reserves the right to order greater or lesser quantities of service under the option provisions. Pricing for these quantities shall be those unit prices currently listed or a mathematical fraction or multiple thereof.

Final and binding notice of intention to exercise an option to extend this contract shall be given in writing to the contractor no later than thirty (30)

*Fiscal Year runs from October 1 through September 30. This contract is approved, would have an operational date as indicated in paragraph D.1. above.

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days prior to the expiration date of service under the basic contract.

E. Liability Provisions - The contractor shall save and hold harmless and indemnify the Government against any and all liability, claims, demands, actions, judgments, and costs of whatsoever kind and nature for the injury or death of any person or persons and for the loss or damage to any property occurring as a result of the negligent acts or omissions of the contractor or contractor personnel while in, upon or about the national cemetery, or while going to or departing from the national cemetery.

F. Deductions for Non-Performance - If the contractor fails to provide services in accordance with the specifications, the Contracting Officer may terminate the contract. Payment will not be made for services not performed. Reduction in payments otherwise due the contractor shall be made for any work not satisfactorily accomplished in accordance with the specifications of the contract as determined by the Contracting Officer.

G. Payment for Services - The contractor shall be paid monthly upon acceptance of services and submission of proper invoices to the COR who will certify the invoices for payment.

Senator CRANSTON. Don, you have experience as Surgeon General of the Navy with contracting out. What was that experience, and how do you look upon it?

Dr. CUSTIS. I had no experience, Senator, in contracting out.

Senator CRANSTON. Wasn't that going on in the Navy while you were there?

Dr. CUSTIS. Not for direct medical care. There was interest in certain offices, elements in the Department of Defense, for the contracting out of entire hospitals, which the Surgeon General at that time unanimously opposed.

As I understand it, even today, that has not been done.

We did have experience in contracting out certain commercial-industrial type services in hospitals, and had a wide spectrum of experience from very poor to good. I've had no experience in contracting for segments of direct health care.

Senator CRANSTON. What kind of services were being contracted out?

Dr. CUSTIS. Word processing, recordkeeping, engineering type services, some of the very things that are identified in our General Counsel's opinion.

Senator CRANSTON. Was there no nutrition or maintenance-type work?

Dr. CUSTIS. No, sir.

Senator CRANSTON. Was the Air Force contracting out some medical services at that time?

Dr. CUSTIS. It's my understanding that the Air Force has not contracted out a whole hospital facility, but has experience in certain segments of health care.

Senator CRANSTON. What portions?

Dr. CUSTIS. There are Air Force representatives in the room, Senator, and I feel obliged to defer to them.

Senator CRANSTON. Were you aware of their work when you were Surgeon General of the Navy?

Dr. CUSTIS. I was aware of the interest on the part of the Air Force in exploring this.

Senator CRANSTON. Was there a lack of similar interest on the part of the Navy?

Dr. CUSTIS. Very much so.

Senator CRANSTON. Why?

Dr. CUSTIS. We were dubious as to whether this would jeopardize the effectiveness of integrated, multidisciplinary health-care delivery team.

Senator CRANSTON. Based on your own experience and knowledge of this area and your professional judgment as a physician, what concerns do you personally have, professionally, regarding contracting out in VA health care facilities?

Dr. CUSTIS. I would just repeat what I've been saying, that I have no concern about contracting the commercial-industrial phases of hospital performance.

My concern lies in the definition of what those may be.

Senator CRANSTON. Yes.

Dr. CUSTIS. And to the extent that one's definition gets into the category of personnel involved in the multidisciplinary team delivering medical care, then I am greatly concerned.

I'm aware of the fact that we are currently forced to go for some professional service contracts, but we do that only in circumstances where we literally are unable to recruit in-house, high-paid professionals, such as pathologists, anesthesiologists, and radiologists.

When we do so, we feel that we have something less than an ideal situation, as regards the quality of patient care. And we pay a high price for it.

Senator CRANSTON. Given the existing OMB statements on the subject, and the legal opinions, do you feel that you have adequate authority and latitude in your capacity as Chief Medical Director to determine appropriately where there could be contracting out and where there should not be?

Dr. CUSTIS. I would answer that affirmatively, Senator, and should you wish, I think Ms. Quandt could add to that response.

Ms. QUANDT. There are several areas in which we are already contracting very broadly in our health-care system. And I think one thing that makes the Department of Medicine and Surgery very different from any of the other Federal health-care systems is the flexibility that Congress has given it through title 38.

We have any number of ways in which we can contract out for service and obtain that service in operating our health-care system, unlike what happens in the Department of Defense or what has happened in Public Health Service.

We are extensively using contractors for window washing, for grounds maintenance and for other activities, which are very definitely commercial and industrial.

Senator CRANSTON. Have formal evaluations been done or are they going to be done?

It's obvious, in window washing, for example, that this may be very, very appropriate. But where other skills are called into play that relate to medical care, it's a different matter.

Have there been evaluations prepared of the various areas where it's working or where there's a question that it's working?

Ms. QUANDT. We're looking at where we are in A-76 now. Since the passage of Public Law 97-66, there will be no further work or evaluation.

We would have to supply for the record any studies that have been done. I don't know of any offhand.

Senator CRANSTON. Don, shouldn't we have a formal assessment of evaluation of the success or inadequacy of the contracting out that is now occurring?

Ms. QUANDT. Our best example would be in laundry, where we have had some rather sad situations in the last 2 fiscal years.

Senator CRANSTON. Yes, that's not what I'm asking. I'd like to ask that there be an assessment made and that we receive a copy.

Dr. CUSTIS. Of our experience?

Senator CRANSTON. Yes. Thank you.

[Subsequently, the Veterans' Administration submitted the following information:]

APPLICABILITY OF OMB CIRCULAR A-76 TO MANAGEMENT FUNCTIONS

The Agency has further considered Senator Cranston's request that we undertake an evaluation of Agency contracting-out. The diversity and magnitude of current VA contracting efforts makes such a study prohibitively expensive and time-con-

suming. We are reluctant to pursue such a study in absence of further guidance from the Committee, and we ask the Committee to defer this request at this time.

Senator CRANSTON. Mr. Cook, what's the status of the AFGE's objections to the Circular A-76 process in the VA?

Mr. COOK. The VA proceeded to publish its internal directives without their concurrence.

Senator CRANSTON. On page 4 of your statement, you mention negative experiences in the 1950's in contracting for laundry services.

Could you give us details for the record on those experiences?

Mr. COOK. Yes, sir, we can furnish specific locations.

[Subsequently, the Veterans' Administration submitted the following information:]

Applicability of OMB Circular A-76 to Management Functions

Contracting Out of Laundry Service in New York

As a result of Bureau of the Budget directives concerning services provided by the government vs. procurement of such services from private enterprise, the laundries at VA medical centers in the Bronx and New York were shut down and the work contracted out in FY 1959. Contracting out the work resulted in additional costs of approximately \$97,000 in FY 1964 and approximately \$427,000 in the succeeding six years after the closing of the two medical center laundries on October 1, 1958. During that time, laundry machinery at the two facilities which cost \$290,000 was idle.

In January 1965, the Comptroller General of the United States advised the Bureau of the Budget and the Veterans Administration of the results of a review conducted by them and proposed that the Administrator of Veterans Affairs reactivate the laundries at the two medical centers and consider the use of in-house laundries at certain other medical centers.

The laundry facility at VAMC New York was reactivated July 1, 1966, after the VA completed an in-depth study of comparative costs between commercial and VA-provided laundry service for the New York Medical Center using FY 1966 workload and commercial laundry rates. The study showed that by providing its own laundry service for the New York Medical Center, the annual savings would be \$44,112, or 21 percent. As a result, the VA notified the New York linen contractor of their intentions to discontinue service effective June 30, 1966. Subsequently, plans were made for VAMC New York to furnish laundry services to VAMC Bronx as a consolidation action. Contract service was discontinued and New York began laundry service to the Bronx Medical Center January 1, 1968. As a result of the New York/Bronx consolidation, \$220,492 in total funds for laundry operations were available for withdrawal from the primary fund allocation for VAMC Bronx in FY 1968.

For the information of the Committee, the Agency submits a Comptroller General's Report (B-13304), dated September 20, 1965, on potential savings through use of government-owned VA laundry facilities, rather than contract services. The report follows in its entirety:

**REPORT TO
THE CONGRESS OF THE UNITED STATES**

**POTENTIAL SAVINGS THROUGH
USE OF GOVERNMENT-OWNED LAUNDRY FACILITIES
AT HOSPITALS
RATHER THAN USE OF CONTRACT SERVICES**

VETERANS ADMINISTRATION



**BY
THE COMPTROLLER GENERAL
OF THE UNITED STATES**

SEPTEMBER 1965



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-133044

SEP 20 1965

To the President of the Senate and the
Speaker of the House of Representatives

Herewith is our report on potential savings through use of Government-owned laundry facilities at Veterans Administration hospitals rather than use of contract services.

On the basis of our review at two Veterans Administration hospitals, we believe that substantial savings could be realized if the hospitals provide their own laundry services, using existing facilities, instead of contracting for such services from commercial laundries. Because of the relationship of our findings at the two hospitals to the general policy of the Government on the use of Government activities to provide services for governmental use, we believe that a reconsideration of the policy's criteria for making cost comparisons in deciding whether services should be contracted out or performed directly by the Government is desirable.

The Veterans Administration operates a nationwide system of hospitals and domiciliaries which, for the most part, provide their own laundry and linen services. In fiscal year 1959, the Veterans Administration closed its laundry operations at five large hospitals and obtained contract services as a pilot test to determine the feasibility of obtaining laundry services from commercial sources. This action was taken to comply with the general policy of the Government, expressed in a series of Bureau of the Budget bulletins, on the use of private enterprise rather than commercial-industrial activities of the Government to provide products or services for governmental use.

Since 1959, three of the five pilot test hospitals have been replaced by new construction without laundry facilities. Our review at the two remaining hospitals, located in the boroughs of Bronx and Manhattan, New York, N.Y., disclosed that additional costs, estimated by us to be about \$97,000 in fiscal year 1964 and about \$427,000 during the 6-year period since the laundries were deactivated in fiscal year 1959, have been incurred by use of contract laundry services rather than Government-owned laundry facilities. Further, Veterans Administration studies show, and many hospital authorities believe, that a

B-133044

hospital-operated laundry is the most desirable means of meeting the requirements for economical, sanitary, and controlled laundry service and is an essential activity of a well-planned hospital.

In making our cost estimates of in-house laundry service, we considered it appropriate to include only those direct and indirect costs that would be incurred by reactivation and operation of the hospital laundry facilities. However, in a Veterans Administration study to determine whether to reactivate the hospital laundry facilities, certain indirect costs and other cost elements not usually associated with Government operations were included in the costs of in-house laundry services to conform to the requirements of Bureau of the Budget Bulletin No. 60-2. By assigning such costs to Government operations, the study showed that no savings would result from reactivation of the hospital facilities, and it was concluded, therefore, that the discontinuance of contract laundry service could not be justified.

In January 1965 we advised the Bureau of the Budget and the Veterans Administration of the results of our review and proposed that the Administrator of Veterans Affairs reactivate the laundries at the two hospitals and consider the use of in-house laundries at certain other hospitals.

On May 13, 1965, the Assistant Director for Management and Organization of the Bureau of the Budget informed us that the Veterans Administration's use of commercial laundry services was in conformance with a general policy of the Bureau that commercial sources should be relied upon for such services unless a compelling reason existed for approving an exception. He stated that extensive studies were made which indicated that total overall costs to the Government would not be increased as a result of applying this policy to laundry services required by some Veterans Administration hospitals but that some of the cost factors considered in these studies were not the same as those used in our computation. He stated, also, that the Bureau is revising its policy, as currently expressed in Bureau of the Budget Bulletin No. 60-2, and that the question of which cost factors should be used is under consideration and that, as soon as this question has been resolved, the Bureau would be in a position to comment more fully on our findings and proposals.

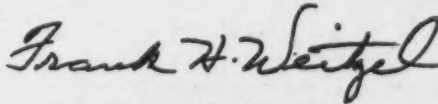
B-133044

By letter dated May 25, 1965, the Deputy Administrator of Veterans Affairs advised us that the agency's policy on operation of laundries is associated with this Bureau of the Budget bulletin and that full consideration will be given to our proposals when the bulletin has been revised.

In determining the costs of a Government operation, the inclusion, as required by Bureau of the Budget Bulletin No. 60-2, of certain indirect costs not incurred by reactivation and operation of the hospital facilities and those cost elements not usually associated with Government operations results, in our opinion, in comparability analyses that do not accurately measure the costs to the Government of using in-house laundry service. We are recommending therefore that the Bureau of the Budget, in connection with the revision of the Bulletin, consider the exclusion from the cost computation of a Government operation those types of costs which, as in the case of these two illustrations, result in unrealistic cost comparisons.

We are reporting this matter for the information of the Congress because of congressional interest in the Bulletin and because of the opportunity the Veterans Administration has to reduce costs and to obtain more desirable laundry service.

Copies of this report are being sent to the President of the United States, the Director of the Bureau of the Budget, and the Administrator of Veterans Affairs.



Acting Comptroller General
of the United States

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REPORT ON
POTENTIAL SAVINGS THROUGH
USE OF GOVERNMENT-OWNED LAUNDRY FACILITIES
AT HOSPITALS
RATHER THAN USE OF CONTRACT SERVICES
VETERANS ADMINISTRATION

INTRODUCTION

The General Accounting Office has made a review of the use of contract laundry services at selected Veterans Administration (VA) hospitals. Our review was made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67) and was performed at the VA Central Office and the Bronx and New York (Manhattan) VA hospitals in New York, N.Y. The review was made at these hospitals because the laundry facilities and equipment were available for reactivation of in-house laundry operations.

Our review dealt primarily with whether laundry services could be provided by existing hospital facilities at savings to the Government. Although we made general comparisons of the respective benefits of in-house and contract laundry services, we did not make a general evaluation of the contracted services.

The VA operates a nationwide system of hospitals and domiciliaries. To meet its responsibility to provide for the proper care and treatment of its hospital patients and domiciliary members, the VA requires each of its hospitals and domiciliaries to maintain an efficient, sanitary, and controlled laundry and linen distribution system. To carry out these requirements, the VA operates 139 laundries providing services to 153 VA hospitals and domiciliaries.

In fiscal year 1964, VA-operated laundries processed 259 million pounds of laundry at a cost of \$13.2 million.

At 16 other VA stations, laundry services are provided by contracts with commercial laundries, and at 2 stations contracts are in force with the Federal Prison Industries. In fiscal year 1964, these commercial laundries and the Federal Prison Industries processed 13 million pounds of laundry for the VA at a cost of \$1.2 million. Thirteen of the stations using contract laundry services were considered too small to economically justify a laundry or did not have a laundry facility when acquired by the VA. This report is concerned primarily with the remaining five hospitals where the laundry facilities were closed in fiscal year 1959 in favor of contracting for laundry services.

The principal officials of the Veterans Administration and Bureau of the Budget concerned with matters discussed in this report are listed in the appendix.

FINDING AND RECOMMENDATIONPOTENTIAL SAVINGS FROM USE OF
GOVERNMENT-OWNED LAUNDRY FACILITIES

On the basis of our review at the Bronx and Manhattan VA hospitals in the city of New York, N.Y., we believe that additional costs, estimated by us to be about \$97,000 in fiscal year 1964 and about \$427,000 during the 6-year period since the hospital laundries were deactivated in fiscal year 1959, have been incurred by the use of contract rather than in-house laundry services. Further, VA studies show, and many hospital authorities believe, that a hospital-operated laundry is the most desirable means of meeting the requirements for economical, sanitary, and controlled laundry service and is an essential activity of a well-planned hospital.

The hospital-operated laundries were deactivated to comply with the general policy of the Government, which was expressed in a series of Bureau of the Budget (BOB) bulletins, on the use of private enterprise rather than commercial-industrial activities of the Government to provide services for governmental use. We believe that, because of the relationship of our findings at the two hospitals to this general policy of the Government, a reconsideration of the policy's criteria for making cost comparisons in deciding whether services should be contracted out or performed directly by the Government is desirable.

Government policy

Current policy on the use of commercial or Government facilities to provide a product or service for governmental use is contained in BOB Bulletin No. 60-2, dated September 21, 1959. This Bulletin, the current successor to earlier Bulletins Nos. 55-4 (1955) and 57-7 (1957) on the same subject, expresses the policy as follows:

"It is the general policy of the administration that the Federal Government will not start or carry on any commercial-industrial activity to provide a service or product for its own use if such product or service can be procured from private enterprise through ordinary business channels."

The Bulletin provides that exceptions to the policy can be made by the head of an agency when it is clearly demonstrated that it is not in the public interest to procure the product or service from private enterprise because (1) national security would call for performance by Government personnel, (2) commercial procurement would involve relatively large and disproportionately higher costs, and (3) commercial procurement would be clearly infeasible, such as, when the product or service is an integral function of the basic mission of the agency or is not available commercially or when commercial procurement is administratively impractical.

Development of VA policy

Pursuant to requirements in Bulletin No. 55-4, the VA made evaluations in 1955 to determine the feasibility of contracting with commercial firms for laundry services at VA hospitals. At that time, 13 VA hospitals and domiciliaries were already contracting for laundry services, principally, because the stations either were too small to economically justify a laundry or did not have a laundry facility when acquired by the VA.

The evaluations showed that, in general, a laundry was an essential part of a well-planned hospital and that VA-operated laundries provided better service at substantially less cost than that provided by contract. It was decided, however, that, because of the individual circumstance at each hospital, a rigid policy regarding laundry services at VA hospitals was impracticable. The VA decided that it would (1) continue to operate laundries at

psychiatric hospitals because of the therapeutic value of having certain patients working in the laundries, (2) not operate laundries at domiciliaries, and (3) continue VA laundries at all other stations until the laundry facilities required major alterations, improvements, or repairs, at which time the merits of using commercial service would be evaluated in each individual case.

In October 1957, the VA requested BOB approval of laundry facilities for its planned replacement hospitals at Jackson, Mississippi, and Nashville, Tennessee, because adequate competition to handle VA hospital laundry did not exist and VA had no assurance of continued availability of commercial laundry service of a quality consistent with hospital requirements.

The BOB advised the VA, however, that it would not approve laundries for these locations nor would it approve funds to construct, enlarge, or modernize laundries at other general or tuberculosis hospitals except where the hospitals were located in rural areas and commercial laundry services were not available. The VA decided, therefore, that (1) design plans for new hospitals at Jackson, Nashville, and Washington, D.C., would be submitted for BOB approval without laundry facilities and (2) contracts for laundry services would be made at the existing Washington, Jackson, Nashville, Bronx, and Manhattan hospitals on a test basis to accumulate operating experience on the cost, practicability, and dependability of using commercial laundry services.

At hearings held before the House Committee on Veterans Affairs in July 1958, considerable discussion took place regarding the VA decision to close its laundries at the five test stations. The Chief Medical Director stated that it was the general belief of the medical profession that laundries are a part of a hospital

operation. He stated further that this matter, under the pressure of Bulletin No. 57-7, was the subject of discussion for some months at the VA and that, finally, a compromise decision was reached to contract for laundry services on a pilot test basis.

Information presented to the committee showed that practically all large hospitals throughout the United States, public and private, operated their own laundries and that numerous advantages accrued from the standpoint of economy and efficiency when the laundry was operated and controlled by the hospital. The committee report on the hearings stated that the VA should be allowed to consider the question of laundry services on the basis of the best principles of medical care that were consistent with economical operation. During the period October 1958 through February 1959, however, the VA closed its laundries at the five test stations. Since 1959, three of the five test hospitals have been replaced by new construction without laundry facilities. At the remaining hospitals, Bronx and Manhattan, the laundry equipment, which cost about \$290,000, has remained idle and in a standby status.

In May 1960, the VA advised the BOB that studies at the five test stations showed that the use of commercial services was feasible but that both feasibility and cost must be considered in making a determination at each individual station. The VA concluded, therefore, that it would adhere to a policy of using commercial services wherever and whenever feasible and in the public interest. This policy, which is still in effect, provides, specifically, that

1. Laundries will not be constructed at new and replacement general and tuberculosis hospitals if adequate commercial competition exists at an economic rate.
2. When existing general or tuberculosis hospital laundries require substantial modernization or replacement of

buildings and/or equipment, or when hospitals are slated for modernization or replacement and the laundry buildings could be used advantageously to avoid additional construction, conversion to commercial service will be made, providing there is adequate competition at an economic rate.

3. Psychiatric hospitals will continue to operate laundries because of the therapeutic value to the patients.

To implement this policy, the VA submitted for BOB approval a proposal to replace hospital laundry operations with commercial laundry services--if, in the opinion of the station directors, competitive commercial laundry sources would be available--at 45 hospitals during the period 1961 through 1974, the time of replacement to be based on the estimated expiration of the useful life of the existing VA laundry equipment at each installation. VA records show that the BOB approved the policy but requested acceleration of the program.

After the 1960 policy was established, the VA made studies of the feasibility and cost of commercial laundry service at approximately 20 locations where hospital construction or modernization was contemplated. At each location, the studies showed that a VA laundry operation would cost considerably less than contracting for laundry service. We were advised that none of the 45 hospitals included in the conversion program have changed to commercial service, largely, because of the economic advantages of continuing the VA-operated laundries.

In April 1962, a VA study of the cost of using VA laundries compared with the cost of using commercial laundry service at the Bronx and Manhattan hospitals showed that annual savings of about \$146,000 in direct costs, excluding the costs of facilities and equipment, could be realized if the two hospitals reactivated their

laundries. The study indicated, in addition, that the use of the VA-operated laundries would improve laundry service and reduce the capital outlay for linen stocks. As a result of this study, the VA decided to reactivate the hospital laundries in the early months of fiscal year 1963.

In October 1962, we requested information from the Chief Medical Director concerning the delay in reactivating the laundries. He advised us that the laundries would be reactivated by July 1, 1963, and that the VA was convinced that the operation of its own laundries provided better service at lower costs. However, after another study in March 1963 at the Bronx hospital, the VA changed its decision because the inclusion of all direct and indirect costs and costs not actually incurred by the Government but required for cost comparison purposes by Bulletin No. 60-2 showed no savings to the Government. It was decided, therefore, not to reactivate the laundries pending an overall VA-wide study by the VA Office of Management and Evaluation.

Bulletin No. 60-2 provides that starting or continuing a Government operation on the grounds that procurement from commercial sources would involve higher costs may be justified only if the costs are analyzed on a comparable basis and the differences are found to be substantial and disproportionately large. The Bulletin requires that, in making cost comparisons, the costs assigned to the Government operation must cover all direct and indirect costs of the Government. It also requires appraisal of elements not usually chargeable to current appropriations, such as interest on the Government's investment, the cost of self-insurance, and exemption from Federal, State, and local taxes, to the extent necessary to put the costs on a comparable basis.

Estimated additional costs at the
Bronx and Manhattan hospitals

On the basis of our comparison of costs of contract and VA-operated laundries at the Bronx and Manhattan hospitals, we estimate that the VA incurred additional costs at these hospitals of about \$97,000 in fiscal year 1964, and about \$427,000 during the 6-year period since the laundries were deactivated in fiscal year 1959, by the use of contract rather than in-house laundry services. The following tabulation shows the estimated additional costs of contract laundry services for fiscal year 1964.

	Fiscal year 1964		
	Total	Bronx	Manhattan
Contract service, actual costs:			
Laundry contract	\$310,600	\$148,700	\$161,900
VA salaries (note a)	93,000	62,400	30,600
Utilities (note a)	<u>2,600</u>	<u>700</u>	<u>1,900</u>
	<u>406,200</u>	<u>211,800</u>	<u>194,400</u>
VA-operated laundry, estimated costs:			
Salaries and related costs			
(note b)	222,900	118,700	104,200✓
Utilities and supplies (note c)	44,200	22,900	21,300
Maintenance and repairs (note b)	19,500	11,100	8,400
Provision for replacement of equipment	<u>22,800</u>	<u>13,800</u>	<u>9,000</u>
	<u>309,400</u>	<u>166,500</u>	<u>142,900</u>
Estimated additional costs of contract laundry service	<u>\$ 96,800</u>	<u>\$ 45,300</u>	<u>\$ 51,500</u>

^aRepresents the costs of VA personnel or utilities used in sorting, marking, and handling linen.

^bBased on the number of positions and grades and cost of supplies estimated by VA station officials to be necessary to reactivate and operate the laundry facilities.

^cEstimated by relating, on an average daily-patient-load basis, the actual costs at the Brooklyn VA hospital to operate its laundry to the Bronx and Manhattan hospitals.

In making our cost comparisons, we considered only those direct and indirect costs that would be incurred by the reactivation and operation of the hospital laundry facilities. We did not consider certain indirect costs that Bulletin 60-2 requires to be considered in comparability analyses--such as, the allocation of office and administrative expenses to the laundry operation, interest on laundry plant and equipment, and depreciation of the laundry buildings--because there would be no appreciable increase in these costs if the laundries were reactivated and because these costs are being incurred by the Government regardless of whether or not the laundry facilities are being used.

In determining costs under in-house operations, we did not include provisions for state and local taxes because the Federal Government is exempt from such taxes and they do not represent an actual cost to the Federal Government. Also, we have not included the loss of Federal income taxes that the contractor may pay because we believe it would not be of sufficient significance to negate the estimated cost advantage of in-house operations.

Our cost comparisons were made on the basis that the Bronx and Manhattan hospitals would each operate a laundry. On the basis of discussions with VA Central Office personnel, it appears, however, that even greater economies may be possible by having one VA laundry facility provide services for both hospitals. We found that 10 VA hospitals receive laundry services from other nearby VA hospitals. The economy in manpower and equipment to be realized by this means of providing laundry service may also be available by consolidating the VA laundry activities at the Bronx and Manhattan hospitals.

Other advantages of VA-operated laundries

Hospital officials advised us that the operation of VA laundries was more desirable because of certain disadvantages inherent in using contract service. They stated that better control and improved service would be obtained by reactivating the VA laundries. For example, we were advised that under contract services the hospitals had no direct control over the laundry once it left the hospital and that, therefore, it was difficult and costly to maintain the controls necessary to guard against theft and misuse of the linen inventory. We were advised, also, that contract laundry services did not offer the flexibility required to meet the needs of the hospital, particularly during periods when there were special rush demands for certain items of linen. Further, because the VA had no direct control over the contractor's operations, it would be more difficult to minimize linen deterioration and damage in the laundry processes and to ensure the proper degree of cleanliness and sanitation.

Officials at both hospitals favored reactivating the VA laundries because of the control and flexibility factors. The director of the Manhattan hospital stated that, in his opinion, the laundry was just as much a part of the hospital's services as the laboratory. Also, we found that many hospital authorities believe that the more desirable means of meeting hospital requirements for economical, sanitary, and controlled linen and laundry service is operating a hospital laundry rather than contracting for the service. Statistics published by the American Hospital Association (AHA) in August 1964 show that 493 or 91 percent of the 541 short-term general and other hospitals with 300 or more beds, registered with the AHA, have hospital-operated laundries. The Bronx and Manhattan

hospitals have operating capacities of about 1,300 and 1,200 beds, respectively.

After our review at the Bronx and Manhattan hospitals, the VA Office of Management and Evaluation in February 1964 completed a VA-wide study of hospital laundry operations, including VA hospitals using contract laundry service. In general the study pointed out that a laundry was an essential part of a well-planned hospital and that implementation of existing VA policy presented the agency with significant administrative problems. The study concluded that (1) VA-operated laundries are more economical, (2) there is a lack of interest on the part of contract laundry operators in doing VA laundry as evidenced by the fact that, at half the VA hospitals using contract service, competitive bidding no longer exists, (3) operational control over cross infection, linen loss or damage, operating costs, and maintenance of a flexible linen service is either sacrificed or too costly when laundry service is obtained by contract, and (4) implementation of existing policy has caused considerable delays in the VA construction program, thereby increasing costs.

The study concludes that, with regard to the programming of new and replacement hospitals, the existing VA policy creates an unnecessary administrative burden on the VA because the source of laundry service must be determined during the early planning stages of a hospital. At that time they would have no certainty that there would still exist, when the hospital is finally activated, the price quotations, capability, or interest of potential contract laundries for doing VA laundry. The study points out that the addition of laundry facilities to hospitals constructed without them results in additional construction and operating costs.

The study recommends that VA policy be revised to exempt laundries from the requirements of Government policy on commercial-industrial activities as set forth in Bulletin No. 60-2. It recommends, also, that the VA operate laundries to provide services to all hospitals and domiciliaries. However, the 1960 policy has continued to remain in effect, and all the 16 stations, including the five test stations, are obtaining laundry service from commercial sources.

Comments of Bureau of the Budget
and Veterans Administration

On January 13, 1965, we advised the BOB and the VA of the results of our review and proposed that the Administrator of Veterans Affairs either reactivate the laundries at the Bronx and Manhattan hospitals, or, if determined feasible, reactivate one of the laundries to provide services to both hospitals. We proposed also that the Administrator consider the use of in-house laundries at other hospitals where similar significant advantages would accrue to the Government.

On May 13, 1965, the Assistant Director for Management and Organization of the BOB advised us that the VA's use of commercial laundry services was in conformance with the general policy of the BOB that commercial sources should be relied upon for such services unless a compelling reason existed for approving an exception. He stated that extensive studies were made which indicated that total overall costs to the Government would not be increased as a result of applying this policy to laundry services required by some VA hospitals but that some of the cost factors considered in these studies were not the same as those used in our computation. He advised us that currently the BOB was inclined to believe that

Federal taxes at least should be considered in making cost comparisons between Government activities and commercial alternatives. He stated also that the BOB was revising its policy, as currently expressed in Bulletin No. 60-2; that the question of which cost factors should be used was under consideration; and that, as soon as this question has been resolved, the Bureau would be in a position to comment more fully on our findings and proposals.

By letter dated May 25, 1965, the Deputy Administrator of Veterans Affairs advised us that the VA policy on operation of laundries is associated with this Bulletin and that full consideration will be given to our proposals when it has been revised.

Conclusion and recommendation

In determining the costs of a Government operation, the inclusion, as required by Bulletin No. 60-2, of certain indirect costs not incurred by reactivation and operation of the hospital facilities and those cost elements not usually associated with Government operations results, in our opinion, in comparability analyses that do not accurately measure the costs to the Government of using in-house laundry service. We recommend therefore that the Bureau of the Budget, in connection with the revision of Bulletin No. 60-2, consider the exclusion from the cost computation of a Government operation those types of costs which, as in the case of these two illustrations, result in unrealistic cost comparisons.

PRINCIPAL OFFICIALS OF THE VETERANS ADMINISTRATION
AND THE BUREAU OF THE BUDGET
CONCERNED WITH MATTERS
DISCUSSED IN THIS REPORT

		<u>Tenure of office</u>	
		<u>From</u>	<u>To</u>
<u>VETERANS ADMINISTRATION</u>			
ADMINISTRATOR OF VETERANS AFFAIRS:			
S. G. Whittier	Dec. 1957	Jan. 1961	
J. S. Gleason, Jr.	Feb. 1961	Jan. 1965	
W. J. Driver	Jan. 1965	Present	
DEPUTY ADMINISTRATOR:			
R. J. Lamphere (acting)	Dec. 1957	Nov. 1958	
F. B. Morse	Nov. 1958	Sept. 1960	
R. J. Lamphere	Sept. 1960	Feb. 1961	
W. J. Driver	Feb. 1961	Jan. 1965	
A. H. Monk (acting)	Jan. 1965	Feb. 1965	
C. F. Brickfield	Feb. 1965	Present	
CHIEF MEDICAL DIRECTOR:			
W. S. Middleton, M. D.	Mar. 1955	Feb. 1963	
H. M. Engle, M. D. (acting)	Mar. 1963	May 1963	
J. H. McNinch, M. D.	June 1963	Present	
<u>BUREAU OF THE BUDGET</u>			
DIRECTOR:			
P. F. Brundage	Apr. 1956	Mar. 1958	
M. H. Stans	Mar. 1958	Jan. 1961	
D. E. Bell	Jan. 1961	Dec. 1962	
K. Gordon	Dec. 1962	June 1965	
C. L. Schultze	June 1965	Present	

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PRINCIPAL OFFICIALS OF THE VETERANS ADMINISTRATION
AND THE BUREAU OF THE BUDGET
CONCERNED WITH MATTERS
DISCUSSED IN THIS REPORT (continued)

		<u>Tenure of office</u>	
		<u>From</u>	<u>To</u>
<u>BUREAU OF THE BUDGET</u> (continued)			
DEPUTY DIRECTOR:			
M. H. Stans	Sept. 1957	Mar. 1958	
R. E. Merriam	Mar. 1958	Sept. 1958	
R. W. Jones	Sept. 1958	Mar. 1959	
E. B. Staats	Mar. 1959	Present	

Senator CRANSTON. What would prevent a recurrence of those negative results today?

Mr. COOK. One of the differences we hope, Senator, was in the 1950's, if we were able to solicit a bid that we could award, we did so.

Our agency policy today says we must have competition before we will consider contracting out. We must have two or more responsible, responsive bidders. Which offers us at least some protection over what happened then.

Senator CRANSTON. Yes, that doesn't necessarily insure that there will be competitive bidding.

Mr. COOK. It isn't foolproof, but it's——

Senator CRANSTON. Later, particularly——

Mr. COOK [continuing]. It's better than what we had.

Senator CRANSTON. Yes.

At page 7 of your statement, you state that 3,900 activities in DM&S affecting 36,000 employees, are subject to review under Circular A-76.

I'd like to ask you to provide us for the record a breakdown by State of the numbers of those employees, showing the numbers and percentages of those employees who are veterans and nonveterans, and among the veterans, if possible, those who have service-connected disabilities and those who are Vietnam-era veterans.

[Subsequently, the Veterans' Administration submitted the following information:]

* Listing of the Estimated Numbers of Veterans, Nonveterans, Disabled Veterans, Vietnam-Era Veterans and Disabled Vietnam-Era Veterans who are potentially subject to A-76 cost comparisons.

<u>State</u>	<u>Nonveterans</u>	<u>Veterans</u>	<u>Disabled Veterans</u>	<u>Vietnam Veterans</u>	<u>Disabled Vietnam Veterans</u>
AL	265	671	111	365	40
AR	350	457	53	258	32
AR	159	378	89	229	63
CA	1,297	2,224	266	1,307	126
CO	168	301	43	165	28
CT	191	200	33	94	12
DC	119	144	14	60	9
DE	58	81	23	44	16
FL	720	866	144	515	90
GA	356	594	72	327	38
IA	287	360	49	167	19
ID	26	64	8	39	3
IL	1,008	1,289	145	594	45
IN	380	417	52	215	24
KS	308	404	48	216	28
KY	225	422	69	266	37
LA	238	435	73	222	27
MA	727	737	142	269	39
MD	390	324	53	143	26
ME	61	226	39	124	21
MI	508	623	103	299	52
MN	349	409	49	205	20

<u>State</u>	<u>Nonveterans</u>	<u>Veterans</u>	<u>Disabled Veterans</u>	<u>Vietnam Veterans</u>	<u>Disabled Vietnam Veterans</u>
MO	353	624	92	315	37
MS	224	463	74	274	34
MT	53	98	14	57	8
NC	322	596	82	326	39
ND	47	76	9	48	8
NE	172	209	44	89	20
NH	83	91	16	45	10
NJ	585	378	59	118	10
NM	70	176	44	106	27
NV	40	73	17	38	5
NY	1,733	2,322	341	1,081	124
OH	711	1,288	146	652	55
OK	101	231	50	132	21
OR	253	410	51	255	33
PA	1,062	1,242	205	578	58
PI	18	0	0	0	0
PR	76	229	37	112	23
RI	39	118	26	39	9
SC	164	244	27	149	18
SD	212	264	23	125	13
TN	315	952	139	528	62
TX	932	1,536	228	816	118
UT	115	113	16	35	3
VA	423	657	105	334	66
VT	47	88	18	53	10
WA	170	397	54	241	33
WI	586	517	54	211	21
WV	182	497	102	275	57
AK	80	156	24	81	11

*This listing includes supervisory personnel who are not directly involved in the activities subject to study.

Senator CRANSTON. Dr. Custis, have the studies in DM&S scheduled prior to enactment of Public Law 97-66 been suspended now due to section 601(b)(2) of that law?

Dr. CUSTIS. Yes, sir.

Senator CRANSTON. What action has been taken to suspend them?

Ms. QUANDT. The medical centers were notified by conference call after the bill was signed by the President that in view of section 601, they should secure any files that they had on studies, but they should stop such work until further notice.

Senator CRANSTON. If you have it, could we have a transcript of that call, for the record, and whatever circular was put out?

Ms. QUANDT. Yes.

Senator CRANSTON. Thank you.

[Subsequently, the Veterans' Administration submitted the following information:]

By telephone conference call on October 23, 1981, the Assistant Chief Medical Director for Administration informed all VA medical center directors of passage of Public Law 97-66. The transcript of that message follows:

"On October 17, 1981, the President signed PL 97-66 entitled 'Veterans Disability Compensation and Pension Amendments of 1981.' Section 601 of this public law amends Title 38, preventing DM&S from expending its funds to complete the cost comparison studies required by OMB Circular A-76 unless Congress provides specific funding for that purpose. The VA was represented in a hearing before the full House Veterans Affairs Committee on October 20 on the subject of A-76. From the reaction at this hearing, nearly unanimous from the committee members, we now have no doubts of the underlying intentions of the House Veterans Affairs Committee as far as Section 601 is concerned. Although A-76 implementation is stopped by this law, any records you have established on your policies, plans and pending studies should be secured and retained indefinitely. Further instruction will come to you after the November 5 hearing when the Senate Veterans Affairs Committee holds its hearing on A-76. If any private business firms raise questions with you on this issue, please refer them to Mr. Cook's Policy and Interagency Staff here at CO, phone number 389-3108. At this point you can stop any work you are doing on A-76. Do not destroy what you have already done. Those employees providing administrative support to DVB must do their A-76 studies."

The Agency has not yet issued a circular or other directive to DM&S facilities. Such a directive will be issued, probably in January 1982.

Senator CRANSTON. Don, in my opening remarks I referred to my concerns about the ominous implications of Circular A-76, in light of the deferral of budget authority, in the major construction account that the President sent the Congress on October 23.

It seems to me that the statement in the justification for that deferral that the funds were being deferred while the administration considers alternative methods for providing readily available, quality medical care for eligible veterans, which I believe must refer to proposals to provide veterans with health care in the private sector at Government expense, may be the first giant step toward shutting down the entire VA hospital system.

I know that Chairman Simpson feels that there is no such implication in that. But I would like to say that, as you know, Administrator Nimmo, at his confirmation hearing, strongly supported the need for separate and independent VA medical care system and with reference to proposals to mainstream veterans' health care stated that those are hazardous ideas that ought not to be pursued.

He also indicated to both the chairman and me that the President's views on these issues were the same as his. That's what Chairman Simpson was referring to.

I'm also aware that you have repeatedly spoken out against mainstreaming proposals. Do you have any comment on what the administration is planning by way of its consideration of these alternative methods, so called, for providing health care to veterans?

Dr. CUSTIS. Senator, I really can shed no light on the meaning or even the implication of that phrase in the deferral request.

I've always felt that the threat—and I do indeed consider it a threat—of mainstreaming is from the private sector, and not from within the Federal establishment.

As a matter of fact, the Deputy Director of OMB, on more than one occasion, has indicated to me that OMB has no interest in mainstreaming veteran care to the private sector.

Senator CRANSTON. Are you concerned about what the real meaning of those words are?

Dr. CUSTIS. I'm confused and concerned, Senator.

Senator CRANSTON. Have you been given any clarification at all on this score since October 2 when the deferral message was sent to Congress?

Dr. CUSTIS. No, sir.

Senator CRANSTON. Kenneth Blaylock, the national president of the AFGE, in his testimony for today's hearings, points out what I view as a significant problem with the implementation of Circular A-76. Namely, the difficulty that is likely to be encountered as the VA attempts to develop statements of work.

Obviously, an incomplete or inaccurate statement of work cannot lead to a good contract.

Mr. Blaylock notes that, for example, the VA's prototype statement of work and dietetics, "fails to make any provision for special diets." Could you explain the reason for that omission?

Mr. Cook. Senator, the prototype statements of work were intended to be just that. General statements of work. And the instructions that were to go with them—do go with them when they go, provide that whatever is required to make it complete and comprehensive at the individual activity will be done.

[Subsequently, the Veterans' Administration submitted the following information:]

The Agency's draft prototype statement of work for hospital food preparation and delivery was constructed to accommodate all forms of food preparation, including modified ("special") diets. The following citations from the SOW address the issue of modified diets: Items 100.0 requires a master menu for regular and modified diets be submitted to the Quality Assurance Evaluator for approval; item 100.1 requires modified diet plans to be developed by a registered dietitian in accordance with the medical center's diet manual; item 104.1 states all foods will be prepared from approved menus; item 104.2 requires standardized recipes for all food preparation.

The prototype establishes sufficient guidelines to assure proper modified ("special") diet meals are delivered. Diabetic menus are written to incorporate as many "regular" foods as possible. In any case, they seldom require individualized preparations.

Senator CRANSTON. What steps will the agency take if the Circular A-76 process actually goes forward, to insure that all statements of work are as complete and accurate as possible?

Mr. COOK. Prototype statements will be reviewed in the headquarters before they're released.

Senator CRANSTON. Thank you very much. I have no further questions now.

Thank you very much.

May we now go to our next witness, Donald Sowle, Administrator, Office of Federal Procurement Policy, OMB. We appreciate your presence. Could I ask that you please summarize and take no more than 5 minutes to do so? Your entire statement will, of course, go in the record. I have to leave shortly. I want to get in a few questions.

TESTIMONY OF DONALD E. SOWLE, ADMINISTRATOR, OFFICE OF FEDERAL PROCUREMENT POLICY, OFFICE OF MANAGEMENT AND BUDGET, ACCOMPANIED BY DARLEEN A. DRUYUN, DEPUTY ASSOCIATE ADMINISTRATOR

Mr. SOWLE. Yes, sir. I'll certainly do that. I would like to introduce my associate here this morning, Ms. Darleen Druyun, who is a staff member at OFPP. One of her main areas is the policy on Circular A-76.

I will summarize my statement. I would like to discuss this morning the merits of OMB Circular A-76 and its application to Veterans' Administration hospitals.

As brief background, I would like to mention that in April of this year, Mr. Ed Harper, Deputy Director of the Office of Management and Budget, wrote to the Veterans' Administration and among other things he pointed out that one of the major goals within this Administration centers on maximizing the efficient expenditure of funds.

OMB's circular, which we're all acquainted with, provides you with one of the necessary tools to achieve this goal.

Mr. Chairman, I would now like to discuss three important issues, as I see them, pertaining to this subject.

No. 1, the proven contracting techniques of the Veterans' Administration can use to insure that qualified contractors are selected to perform support-type hospital services; second, the application of the circular to the VA's mission of providing direct medical care to

qualified veterans; and finally, the private sector's use of contract services in the health-care field.

With respect to the proven contracting techniques, there are three critical phases in the contracting process which insure either success or failure in obtaining products or services needed by the Government.

First, developing a statement of work is one of the most critical elements in the process. Our current policy provides that the work statement should clearly state what is to be done and provide performance standards for each task in the statement of work.

It is these two elements, clearly stated requirements and performance standards, that establish the necessary baseline to select the qualified contractor.

These two elements also provide the basis upon which Government inspection is made to insure quality contractor performance.

The second critical aspect in the contracting process is the selection of a qualified contractor. There are several techniques available for this step, including detailed technical evaluations, and pre-award surveys to insure that a qualified and responsible contractor is selected.

Every contracting officer has the right and indeed the obligation, to make a positive determination that a bidder can satisfactorily perform the requirement prior to award of the contract.

If management, technical or special requirements are critical factors, the contracting officer, together with those the contractor will provide, can evaluate and examine the contractor's proposal in such areas as management and staffing plans, qualifications of the contractor's key personnel, approaches to quality control, ability and plan to provide an orderly phase-in, understanding of technical factors associated with the service, strike contingency plans, and the contractor's ability to meet the standards of the Joint Committee on Accreditation of Hospitals.

The third critical contracting point is a determination of whether the contractor is satisfactorily performing the work for which he has contracted.

Again, I would like to point out that a sound statement of work with written performance standards and selection of qualified contractors will be an effective safeguard against poor performance.

When one adds to this the quality assurance techniques required of the contractor, there is no reason to expect less than satisfactory, high quality performance.

Now, the second issue I would like to discuss briefly, pertains to the VA Counsel's determination that direct medical care is not applicable under Public Law 79-293, title 38, and also that OMB supports the decisions and the conclusions reached by the Counsel of the VA.

We are convinced that contracting out of indirect support care services and custodial services will lead to better patient care. For example, in the event of an emergency, the contractor has more flexibility to perform additional requirements by immediately hiring new people, as opposed to going through the civil service system.

It seems to us, Mr. Chairman, there is no logical business, medical or professional reason why support services to VA hospitals

cannot be contracted out, when veterans' care can be improved at less cost to the taxpayer.

The third and final issue I wish to address is the private sector use of contract services in the health-care area. In July 1981, the periodical entitled "Modern Healthcare," there is a very enlightening article on this subject entitled "Contract Management Survey." Highlights of the article are that some 4,079 hospital and health-care facility departments were managed by outside contractors, as well as other data which I think, should be of importance to this Committee.

I planned to say a few words about the Air Force experience, but I understand you do have a DOD witness here this morning. And so I'll leave that to them.

We at OMB are very much concerned about restrictions on opportunities to improve veterans' care at potential cost savings contained in section 601 of the recent bill that you referred to earlier.

As indicated by the President when he signed the bill, we will work with this committee and the VA to find a mutually agreeable approach to the application of the A-76 policy. We firmly believe that the best interests of the VA will be served by repealing the impediments to A-76 implementation contained in section 601.

Senator CRANSTON. Thank you very much.

Mr. SOWLE. Yes, sir.

[The prepared statement of Donald E. Sowle, Administrator, Office of Federal Procurement Policy, Office of Management and Budget, and the response of the Office of Management and Budget to followup questions submitted by Hon. Alan K. Simpson and Hon. Alan Cranston, follow:]

PREPARED STATEMENT OF DONALD E. SOWLE, ADMINISTRATOR, OFFICE
OF FEDERAL PROCURMENT POLICY, OFFICE OF MANAGEMENT AND
BUDGET

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE: .

THANK YOU FOR INVITING ME HERE TODAY. THE OFFICE OF MANAGEMENT AND BUDGET APPRECIATES THE OPPORTUNITY TO PRESENT ITS VIEWS ON THE VETERANS ADMINISTRATION'S IMPLEMENTATION OF OMB CIRCULAR NO. A-76. I WOULD LIKE TO CENTER MY DISCUSSION ON THE GENERAL FEATURES OF THE CIRCULAR AND THE SPECIFIC IMPLICATION OF THESE FEATURES ON THE VETERANS ADMINISTRATION.

I AM SURE YOU ARE AWARE THAT THE POLICY IN THE CIRCULAR IS NOT A NEW ONE. SINCE 1955 EACH ADMINISTRATION HAS EXPRESSED A GENERAL POLICY OF RELIANCE ON THE PRIVATE SECTOR FOR THE GOODS AND SERVICES NEEDED TO SUPPORT THE ACCOMPLISHMENT OF AGENCY MISSIONS. THE MOST RECENT EXPRESSION OF THIS POLICY WAS PUBLISHED IN 1979. THE POLICY WAS REEMPHASIZED BY THIS ADMINISTRATION IN APRIL OF THIS YEAR WHEN THE DEPARTMENTS AND AGENCIES WERE DIRECTED BY OMB TO TAKE VIGOROUS ACTION IN SUPPORT OF THIS LONGSTANDING POLICY.

THE SALIENT FEATURES OF THE CURRENT POLICY I BELIEVE ARE REFLECTED IN THE IMPLEMENTATION OF THE POLICY BY:

- RECOGNIZING THAT THE ADMINISTRATION AND THE AMERICAN PEOPLE EXPECT EFFICIENCY IN GOVERNMENT OPERATIONS, BUT SPECIFYING THAT ACTIVITIES WILL NOT BE CONVERTED FROM IN-HOUSE TO CONTRACT PERFORMANCE UNLESS THE COST SAVINGS WILL BE SUFFICIENT TO JUSTIFY THE CHANGE.
- PROVIDING A COST DIFFERENTIAL, EQUAL TO 10 PERCENT OF GOVERNMENT PERSONNEL-RELATED COSTS, FAVORING CONTINUATION OF PRESENT IN-HOUSE ACTIVITIES.
- ENSURING THAT ALL COST ANALYSES WILL BE COMPREHENSIVE AND EQUITABLE BY PRESCRIBING USE OF A COST COMPARISON HANDBOOK CONTAINING A DETAILED SET OF INSTRUCTIONS.
- REQUIRING AGENCIES TO PUBLISH AN ADVANCE SCHEDULE SHOWING WHEN ACTIVITIES WILL BE REVIEWED, SO THAT ALL THOSE AFFECTED WILL BE APPRISED.

ADDITIONAL EFFICIENCY IS ACHIEVED BY:

- REQUIRING THAT CONTRACTS FOR SERVICES BE REVIEWED, UPON EXPIRATION OF THE CONTRACT, TO DETERMINE IF IT IS STILL COST EFFECTIVE.

- REQUIRING AGENCIES TO MAKE ALL INFORMATION ABOUT THE PROGRAM SUCH AS INVENTORIES, REVIEW SCHEDULES, AND RESULTS OF REVIEWS AVAILABLE TO ALL INTERESTED PARTIES, INCLUDING EMPLOYEES AND THEIR BARGAINING REPRESENTATIVES. -
- INSTRUCTING EACH AGENCY TO ESTABLISH A PROCEDURE FOR REVIEW OF ALL APPEALS SUBMITTED BY AFFECTED PARTIES. THE PROCEDURE MUST PROVIDE FOR AN EXPEDIENT RULING BY AN OFFICIAL OF EQUAL OR HIGHER LEVEL THAN THE OFFICIAL APPROVING THE ORIGINAL DECISION.
- ENCOURAGING AGENCIES TO REORGANIZE IN-HOUSE ACTIVITIES FOR MAXIMUM EFFICIENCY PRIOR TO MAKING A COST COMPARISON WITH THE PROPOSED CONTRACT PERFORMANCE.
- REQUIRING EACH CONTRACT AWARDED FOR WORK PREVIOUSLY PERFORMED IN-HOUSE TO INCLUDE A CLAUSE GIVING DISPLACED GOVERNMENT EMPLOYEES A RIGHT OF FIRST REFUSAL OF EMPLOYMENT WITH THE CONTRACTOR FOR POSITIONS IN WHICH THEY ARE QUALIFIED.

THE CIRCULAR FURTHER RECOGNIZES IN ITS IMPLEMENTATION THOSE FEDERAL LAWS AND POLICIES WHICH DIRECTLY AFFECT IT. SPECIFICALLY:

- ALL SERVICE CONTRACT EMPLOYEES MUST BE PAID AT LEAST THE WAGES AND FRINGE BENEFITS PREVAILING FOR SIMILAR WORK IN THE LOCALITY, AS DETERMINED BY THE DEPARTMENT OF LABOR.

- EMPLOYMENT PREFERENCE MUST BE GIVEN UNDER CONTRACTS TO DISADVANTAGED PERSONS AND VETERANS, COMPARABLE TO REQUIREMENTS FOR FEDERAL EMPLOYMENT.

- ALL DISPLACED FEDERAL EMPLOYEES ARE GIVEN PRIORITY PLACEMENT CONSIDERATION IN OTHER GOVERNMENT POSITIONS, WITH GRADE RETENTION FOR TWO YEARS AND CONTINUING PAY AT THE SAME RATE IF ASSIGNED TO A LOWER GRADE.

THOSE ARE THE MAIN FEATURES OF THE POLICY RELATING TO RELIANCE ON THE PRIVATE SECTOR.

IN APRIL OF THIS YEAR, MR. ED HARPER, THE DEPUTY DIRECTOR OF THE OFFICE OF MANAGEMENT AND BUDGET, WROTE TO THE VETERANS ADMINISTRATION. AMONG OTHER THINGS, HE POINTED OUT THAT:

"ONE OF THE MAJOR GOALS WITHIN THIS ADMINISTRATION CENTERS ON MAXIMIZING THE EFFICIENT EXPENDITURE OF FUNDS. OMB CIRCULAR A-76, "POLICIES FOR ACQUIRING COMMERCIAL OR INDUSTRIAL PRODUCTS AND SERVICES NEEDED BY THE GOVERNMENT," PROVIDES YOU WITH ONE OF THE NECESSARY TOOLS TO ACHIEVE THIS GOAL. THIS ADMINISTRATION STRONGLY SUPPORTS THE GENERAL POLICY OF RELIANCE ON COMPETITIVE PRIVATE ENTERPRISE TO SUPPLY THE PRODUCTS AND SERVICES NEEDED BY THE GOVERNMENT. THROUGH PROPER AND EFFECTIVE IMPLEMENTATION OF THE CIRCULAR

YOU WILL BE ABLE TO ACHIEVE ECONOMIES AND EFFICIENCIES
IN OPERATING COMMERCIAL-INDUSTRIAL TYPE ACTIVITIES BY:

- DETERMINING THE LEAST COST METHOD OF PROVIDING
ESSENTIAL SERVICES (CONTRACT OR IN-HOUSE).
- STREAMLINING EXISTING GOVERNMENT ORGANIZATIONS,
ENSURING THEY ARE ORGANIZED AND STAFFED FOR THE
MOST EFFICIENT PERFORMANCE.
- REDUCING LONG-RANGE FISCAL OBLIGATIONS THROUGH
REDUCTIONS IN THE FEDERAL WORK FORCE WHEN COST
COMPARISONS SHOW A CONTRACT OPERATION IS MORE
COST EFFECTIVE.
- ENHANCING PRODUCTIVITY THROUGH THE DEVELOPMENT
OF MEASURABLE JOB STANDARDS."

THERE ARE SEVERAL ISSUES I WOULD LIKE TO CENTER MY
DISCUSSIONS ON TODAY. THESE ARE:

- O PROVEN CONTRACTING TECHNIQUES THE VETERANS
ADMINISTRATION (VA) CAN USE TO ENSURE QUALIFIED
CONTRACTORS ARE SELECTED TO PERFORM SUPPORT TYPE
HOSPITAL SERVICES;

- O THE APPLICATION OF THE CIRCULAR TO THE VA'S MISSION OF PROVIDING DIRECT MEDICAL CARE TO QUALIFIED VETERANS; AND
- O THE PRIVATE SECTOR'S USE OF CONTRACT SERVICES IN THE HEALTH CARE FIELD.

WITH RESPECT TO THE FIRST ISSUE, LET ME STATE THAT THE PROPER USE OF PROVEN CONTRACTING TECHNIQUES WILL ASSURE THAT RESPONSIVE CONTRACTS ARE ENTERED INTO AND THAT THE GOVERNMENT IS SATISFIED WITH THE SERVICE OR PRODUCT ACQUIRED. THERE ARE THREE CRITICAL PHASES IN THE CONTRACTING PROCESS WHICH ENSURE EITHER SUCCESS OR FAILURE IN OBTAINING PRODUCTS OR SERVICES NEEDED BY THE GOVERNMENT. THESE ARE:

- O DEVELOPING A STATEMENT OF WORK;
- O SELECTING A QUALIFIED CONTRACTOR; AND
- O EVALUATING CONTRACTOR PERFORMANCE.

I WOULD LIKE TO BRIEFLY DISCUSS EACH ONE OF THESE ELEMENTS.

DEVELOPING A STATEMENT OF WORK IS ONE OF THE MOST CRITICAL ELEMENTS IN THE PROCESS AND IS RECOGNIZED AS SUCH. OUR CURRENT POLICY PROVIDES THAT THE WORK STATEMENT SHOULD CLEARLY STATE

WHAT IS TO BE DONE AND PROVIDE PERFORMANCE STANDARDS FOR EACH TASK IN THE STATEMENT OF WORK. IT IS THESE TWO ELEMENTS -- CLEARLY STATED REQUIREMENTS AND PERFORMANCE STANDARDS -- THAT ESTABLISH THE NECESSARY BASELINE TO ASSURE EFFECTIVE COMMUNICATION OF THE GOVERNMENT'S REQUIREMENTS AND ESTABLISH THE CRITERIA THAT CAN BE USED TO SELECT A QUALIFIED CONTRACTOR. THESE TWO ELEMENTS ALSO PROVIDE THE BASIS UPON WHICH GOVERNMENT INSPECTION IS MADE TO ENSURE QUALITY CONTRACTOR PERFORMANCE.

LAST YEAR OFPP PUBLISHED A PAMPHLET ON WRITING AND ADMINISTERING PERFORMANCE STATEMENTS OF WORK FOR SERVICE CONTRACTS. THIS DOCUMENT WAS BASED ON EXTENSIVE FIELD EXPERIENCE. IT WAS THOROUGHLY TESTED IN HOSPITAL SERVICES PRIOR TO ITS ORIGINAL PUBLICATION BY THE DEPARTMENT OF THE AIR FORCE AND SUBSEQUENTLY ADOPTED AS A METHOD THAT SHOULD BE USED GOVERNMENT-WIDE. I AM GRATIFIED TO REPORT THAT THE DEPARTMENT OF THE MEDICINE AND SURGERY IN THE VA HAS ADOPTED THIS HIGHLY SUCCESSFUL APPROACH FOR WORK STATEMENT PREPARATION FOR MANY OF THEIR REQUIREMENTS SUCH AS CUSTODIAL SERVICES.

THE SECOND CRITICAL ASPECT IN THE CONTRACTING PROCESS IS THE SELECTION OF A QUALIFIED CONTRACTOR. THERE ARE SEVERAL TECHNIQUES AVAILABLE FOR THIS STEP, INCLUDING THE PERFORMANCE OF TECHNICAL EVALUATIONS AND PREAWARD SURVEYS, TO ENSURE A QUALIFIED AND RESPONSIBLE CONTRACTOR IS SELECTED. EVERY

CONTRACTING OFFICER HAS THE RIGHT AND, INDEED, THE OBLIGATION TO MAKE A POSITIVE DETERMINATION THAT A BIDDER CAN SATISFACTORILY PERFORM THE REQUIREMENT PRIOR TO AWARD OF A CONTRACT. IF MANAGEMENT, TECHNICAL, OR SPECIAL REQUIREMENTS ARE CRITICAL FACTORS, THE CONTRACTING OFFICER, TOGETHER WITH THOSE THE CONTRACTOR WILL SERVE, CAN EVALUATE AND EXAMINE THE CONTRACTOR'S PROPOSAL IN SUCH AREAS AS MANAGEMENT AND STAFFING PLANS; QUALIFICATIONS OF THE CONTRACTOR'S KEY PERSONNEL; APPROACHES TO QUALITY CONTROL; ABILITY AND PLAN TO PROVIDE AN ORDERLY PHASE-IN; UNDERSTANDING OF TECHNICAL FACTORS ASSOCIATED WITH THE SERVICE; STRIKE CONTINGENCY PLANS; AND, IN THE HOSPITAL ENVIRONMENT, THE CONTRACTOR'S ABILITY TO MEET THE STANDARDS OF THE JOINT COMMITTEE ON ACCREDITATION OF HOSPITALS.

THE THIRD AND FINAL CRITICAL POINT IN THIS PROCESS IS A DETERMINATION OF WHETHER THE CONTRACTOR IS SATISFACTORILY PERFORMING THE CONTRACT. OVER THE PAST FEW MONTHS, CONCERN HAS BEEN EXPRESSED THAT CONTRACTOR SERVICES MAY BE UNSATISFACTORY BECAUSE OF SHODDY WORKMANSHIP. AGAIN, I WOULD LIKE TO POINT OUT THAT A SOUND STATEMENT OF WORK WITH WRITTEN PERFORMANCE STANDARDS AND THE SELECTION OF QUALIFIED CONTRACTORS WILL BE AN EFFECTIVE SAFEGUARD AGAINST POOR PERFORMANCE. WHEN ONE ADDS TO THIS THE QUALITY ASSURANCE TECHNIQUES REQUIRED OF THE CONTRACTOR, THERE IS NO REASON TO EXPECT LESS THAN SATISFACTORY, HIGH QUALITY PERFORMANCE. IN THE EVENT PROBLEMS SHOULD ARISE, EVEN WITH THESE SAFEGUARDS, THERE ARE AMPLE REMEDIES IN

THE PROCUREMENT PROCESS. THESE RANGE FROM MONETARY DEDUCTIONS FROM PAYMENTS DUE TO DEFAULTING THE CONTRACTOR. THESE REMEDIES HELP ASSURE THAT THE GOVERNMENT RECEIVES WHAT IT CONTRACTED FOR AND THAT WE ONLY PAY FOR WHAT WE RECEIVE.

THE SECOND ISSUE I WOULD LIKE TO BRIEFLY ADDRESS AND ONE WHICH IS OF GREAT CONCERN TO THIS COMMITTEE IS THE APPLICATION OF THE CIRCULAR TO VA'S MISSION OF PERFORMING DIRECT MEDICAL CARE. AS I MENTIONED EARLIER, THE REVISED CIRCULAR WAS PUBLISHED IN MARCH 1979 AND APPLIES TO ALL FEDERAL AGENCIES, INCLUDING THE VETERANS ADMINISTRATION. THERE ARE SEVERAL AGENCIES, IN ADDITION TO VA, WHICH, AS A PART OF THEIR MISSION, PROVIDE HEALTH SERVICES. THE APPLICATION OF THE CIRCULAR TO THOSE ACTIVITIES LISTED IN ATTACHMENT A IS A DETERMINATION MADE BY EACH AGENCY HEAD. IN IMPLEMENTING THE CIRCULAR, AGENCY HEADS EXAMINE SUCH AREAS AS EXISTING STATUTES AND INDIVIDUAL FUNCTIONS TO ASSURE THEY ARE NOT INHERENTLY GOVERNMENTAL OR OTHERWISE PRECLUDED FROM BEING CONTRACTED. IN THE CASE OF THE VA, THEIR GENERAL COUNSEL, IN AN OPINION, DATED MARCH 21, 1980, CONCLUDED THAT CONTRACTING OUT DIRECT PATIENT CARE IS PRECLUDED BY LAW UNDER TITLE 38 AND P.L. 79-293 AND, THEREFORE, MUST BE PERFORMED BY GOVERNMENT PERSONNEL. HOWEVER, THEY ALSO CONCLUDED THAT SUPPORT ACTIVITIES NOT DIRECTLY RELATED TO PATIENT CARE ARE SUBJECT TO THE PROVISIONS OF THE CIRCULAR. I WOULD LIKE TO STATE THAT OMB SUPPORTS THIS OPINION OF THE VA.

THE FINAL AREA I WISH TO ADDRESS IS THE PRIVATE SECTOR'S USE OF CONTRACT SERVICES IN THE HEALTH CARE ARENA. IN THE JULY 1981 PERIODICAL ENTITLED MODERN HEALTHCARE THERE IS A RATHER ENLIGHTENING ARTICLE ON THIS SUBJECT ENTITLED "CONTRACT MANAGEMENT SURVEY." THE HIGHLIGHTS OF THIS ARTICLE ARE:

- O SOME 4,079 HOSPITAL AND HEALTH CARE FACILITY DEPARTMENTS WERE MANAGED BY OUTSIDE CONTRACTORS IN 1980;
- O COST CONTAINMENT PRESSURES ARE THE PRIMARY FACTORS FOR THE USE OF CONTRACT SERVICES IN CLINICAL AND NONCLINICAL AREAS;
- O THE SERVICES MOST FREQUENTLY CONTRACTED FOR ARE: HOUSEKEEPING, FOOD SERVICE, RESPIRATORY THERAPY, PLANT OPERATIONS MAINTENANCE, PHARMACY, LAUNDRY AND OTHER SERVICES; AND FINALLY
- O CONTRACTING OUT SUPPORT SERVICES "ALLOWS A HOSPITAL TO CONCENTRATE ITS ENERGIES ON ITS MAIN PURPOSE -- HEALING THE SICK."

I AM SURE THIS COMMITTEE IS CONCERNED ABOUT THE PROGRAM'S IMPACT ON NOT ONLY THE VETERANS ADMINISTRATION BUT ALSO THE IMPACT ON THE VETERANS FOR WHOM THESE SERVICES ARE PROVIDED. TO ALLAY YOUR CONCERNS IN THIS AREA, I WOULD LIKE TO DRAW UPON THE

EXPERIENCE OF THE AIR FORCE, WHICH HAS HAD A CONSIDERABLE AMOUNT OF INVOLVEMENT IN CONTRACTING FOR SERVICES IN SUPPORT OF THEIR HOSPITALS. AS AN EXAMPLE, BASED ON THE AIR FORCE IMPLEMENTATION OF THE HOSPITAL ASEPTIC MANAGEMENT SERVICES PROGRAM FOR CUSTODIAL SERVICES, SUBSTANTIAL SAVINGS HAVE BEEN REALIZED AND, MORE IMPORTANT, PATIENT CARE HAS IMPROVED BECAUSE PERSONNEL WERE FREED UP FOR OTHER MORE CRITICAL USES. IT IS ALSO INTERESTING TO NOTE THAT THE AIR FORCE RECENTLY CONVERTED TWO HOSPITAL CUSTODIAL FUNCTIONS TO CONTRACT BASED ON A-76 COST COMPARISONS, WHICH SHOWED CONTRACT OPERATIONS TO BE LESS EXPENSIVE BY A MARGIN OF 60 PERCENT IN A LARGE REGIONAL HOSPITAL AND 25 PERCENT IN A SMALL HOSPITAL. AS A RESULT OF THESE TWO COST STUDIES, THE AIR FORCE HAS CONVERTED ALL OF ITS HOSPITAL CUSTODIAL SERVICES IN THE CONTINENTAL UNITED STATES TO CONTRACT. THE COST SAVINGS ANTICIPATED CONTINUE TO BE REALIZED. PROFESSIONAL AND PARA PROFESSIONAL PERSONNEL HAVE BEEN FREED FOR IMPROVED PATIENT CARE AND THE LEVEL OF CLEANLINESS BOTH IN APPEARANCE AND ASEPSIS REMAINS HIGH.

WE IN OMB ARE VERY MUCH CONCERNED WITH THE LOSS OF MANAGEMENT FLEXIBILITY AND POTENTIAL COST SAVINGS AS A RESULT OF THE LANGUAGE CONTAINED IN SECTION 601 OF THE "VETERANS' DISABILITY COMPENSATION, HOUSING AND MEMORIAL BENEFITS AMENDMENTS OF 1981" BILL. AS INDICATED BY THE PRESIDENT WHEN HE SIGNED THE BILL, WE WILL WORK WITH YOU TO ALLAY YOUR CONCERNS AND FIND A MUTUALLY AGREEABLE APPROACH TO THE APPLICATION OF THE

CIRCULAR'S PROVISIONS TO THE VA. WE FIRMLY BELIEVE THAT THE BEST INTERESTS OF THE VA WILL BE SERVED BY REPEALING THE IMPEDIMENTS TO A-76 IMPLEMENTATION CONTAINED IN SECTION 601.

MR. CHAIRMAN, I HOPE THAT MY COMMENTS HAVE BEEN HELPFUL IN PORTRAYING THAT THE INTENDED APPLICATION OF OUR GENERAL POLICY OF RELYING ON THE COMPETITIVE PRIVATE SECTOR IS IN THE BEST INTERESTS OF THE VA AND THE VETERANS WHO DESERVE OUR UPMOST CONCERN. I ALSO BELIEVE THAT BY SERVING THE VETERANS WE ARE ALSO SERVING THE TAXPAYER THROUGH MORE EFFICIENT AND EFFECTIVE OPERATIONS OF VETERAN CARE FACILITIES AND SUPPORT OPERATIONS.

I WILL BE MOST PLEASED TO RESPOND TO ANY QUESTIONS YOU MAY HAVE AT THIS TIME.

THANK YOU.

RESPONSE OF THE OFFICE OF MANAGEMENT AND BUDGET TO WRITTEN QUESTIONS SUBMITTED

BY HON. ALAN K. SIMPSON, CHAIRMAN OF THE SENATE COMMITTEE ON VETERANS'

AFFAIRS

Q.1. There is some uncertainty about the reliability of the statement of work as a device for guaranteeing full and satisfactory performance by the contractor. GAO has identified two major problem areas involving statements of work: the problem of an incomplete statement, as exemplified by the situation of the Air Force Academy's disastrous contract for custodial services, and the problem of an unrealistically low cost estimate by the bidding contractor, as exemplified by the comprehensive contract at the Hawthorne Army Ammunition Plant in Nevada. How do you respond to these concerns, and what safeguards does A-76 contain to minimize the risk of inadequate performance due to improperly drafted statements of work?

A.1. Circular A-76 policy requires the preparation of a sufficiently precise work statement with performance standards that can be monitored for either mode of performance -- contract or in-house.

OFPP Pamphlet No. 4, "A Guide for Writing and Administering Performance Statements of Work for Service Contracts," implements this policy and describes a systematic means for developing statements of work (SOW) and quality assurance surveillance plans. So that the Government can precisely define and measure quality, the pamphlet presents an analytical method of identifying and stating requirements in such a way that the SOW will state accurately the Government's minimum requirements. The pamphlet also explains how to assure that the contractor has actually performed the services required. In the cases cited in your question, the Government apparently did not follow the analytical approach in Pamphlet

No. 4. If they had, the SOWs would have been properly prepared.

We plan to make Pamphlet No. 4 Supplement No. 2 to Circular A-76 in the near future. We have also made the pamphlet part of our A-76 training program, and it has been available to the agencies since October 1980.

Q.2. As pointed out to the panel that preceded you, Title 38, unlike Title 10, requires the establishment and maintenance of a "complete medical and hospital service." Why is this provision not regarded as conferring upon the entirety of DM&S the status of Governmental function for purposes of A-76?

A.2. As stated in OMB's formal testimony, the Circular leaves it to the agency head to determine when certain activities would be precluded by law from the Circular's provisions. The VA's General Counsel, in an opinion dated March 21, 1980, concluded that contracting out direct patient care is precluded by law under Title 38 and P.L. 79-293 and, therefore, must be performed by Government personnel. However, they also concluded that support activities not directly related to patient care are subject to the provisions of the Circular. OMB supports this opinion of the VA.

Q.2A. You have urged the repeal of Section 601 of P.L. 97-66, the Veterans' Disability Compensation, Housing and Memorial Benefits Amendments of 1981.

Am I correct in interpreting this suggestion to mean that you would recommend dipping into the limited medical care account funds to pay for cost comparison studies which may determine that contracting out is not cost effective in some or all instances?

A.2A. No. The cost of conducting OMB Circular No. A-76 cost studies is considered a normal management cost, properly paid for out of existing overhead accounts. Also, funds could be specifically appropriated for this purpose or "borrowed" against anticipated savings resulting from conversions.

By law, agency heads are charged with the fiduciary responsibility of meeting their agency mission in the most economical manner. The pursuit of this objective should involve a constant search for more cost effective options for providing authorized levels of service. Circular A-76 simply prescribes a formal, structured approach to meeting this fiduciary and management mandate. Experience has shown that the savings resulting from conversions has far exceeded the one-time costs of conducting the studies.

Q.3. In cases where a contractor either defaults or breaches the terms of the contract, standard contract remedies enforceable through the courts might be adequate in a purely monetary sense, but there are certain indirect care areas such as food preparation or laundry where even a relatively brief disruption of service can have an appreciable effect on direct patient care. What additional remedies does A-76 provide that would be effective to avoid disruption in such time-sensitive areas?

A.3. The Circular provides that a contract must be monitored to ensure performance. This is accomplished through contract administration and is addressed in Federal Procurement Regulations. Part of contract administration is development of contingency plans to minimize possible disruptions. For example, if an agency desires, it can include a clause within the contract requiring the contractor to develop a strike contingency plan. In the plan, the contractor would have to demonstrate what actions would be taken to effectively mitigate the effects of a strike and to ensure continuity. This procedure has worked well in the past, and we are unaware of any evidence supporting the contention that strikes or other disruptions are a pervasive threat to Government contract operations. Prudent agency management would ensure a contingency plan was in effect, regardless of the mode of performance -- contract or in-house.

Q.4. A-76 states that estimates for the cost of Government performance should be based on a cost factor for Federal employee retirement benefits of 20.4 percent. How do you respond to the charge of Kenneth Blaylock, President of AFGE, that this is a career estimate and should not be compared to the contractor's estimate of the cost of retirement benefits simply during the term of the contract?

A.4. Mr. Blaylock's assumption is incorrect. The 20.4 percent retirement estimate is a current expense and is applicable to all eligible Federal employees, not just

those who work to retirement. Many other civil servants may leave Government service before they are eligible to draw retirement benefits. The length of service for these employees was also considered in developing the 20.4 percent factor.

Q.5. The GAO has recommended that there are two areas in which the A-76 guidelines appear to need revisions to enhance comparability inequity in making cost comparisons. They concluded that the rules concerning the treatment of unoccupied in-house positions and the adjustment of in-house personnel costs for inflation tend to favor contracting out. How has OMB responded to this recommendation?

A.5. We have reviewed the guidelines for costing out unoccupied in-house positions and inflation of personnel costs for in-house employees, as recommended in the GAO report. Based on this review, we plan issuing a change to the Cost Comparison Handbook which provides that in-house personnel costs will only be inflated in the outyears for those personnel not in positions that would be covered by the Service Contract Act or some form of economic price adjustment clause. This change to the Handbook was made by DOD when they implemented the revised Circular in April 1980.

Our review of the wage-grade steps required to be used when costing out unoccupied in-house positions revealed that they are equitable and require no revisions. This

decision was based on recent statistical data obtained from the Office of Personnel Management.

Q.6. The Veterans Administration has the best overall record among all Federal agencies of hiring veterans. If, in compliance with A-76, a large number of activities in the VA, and particularly with the Department of Medicine and Surgery, are contracted out, thousands of veterans currently employed by VA may lose their jobs. What steps will be taken to ensure that veterans, especially those hired under veterans preference authority, are hired by private contractors to fill jobs that are created by such contracts?

A.6. Paragraph 10 of the Circular requires agencies to include a provision in the contract that gives Federal employees, displaced as a result of conversion to contract performance, the right of first refusal for employment openings on the contract in positions for which they are qualified.

Federal Procurement Regulations require contractors with contracts in excess of \$10,000 to take affirmative action in employing veterans, precludes discrimination, and requires listing of openings with local employment offices. In this respect, the requirements are roughly similar to those placed on the Federal Government as an employer.

We believe that the veterans preference clause in Federal contracts, when taken in conjunction with other contract

clauses relating to equal employment opportunity, veteran's preference, and hiring the handicapped, and the unique Circular A-76 clause giving displaced employees the right of first refusal, offer a very favorable employment opportunity for veterans. The net effect of the right of first refusal clause for procurements related to Circular A-76 cost studies is to give absolute hiring preference to qualified displaced Federal employees that are veterans. Thus, we do not believe any further action is necessary to enhance veterans' employment opportunities under contracts.

RESPONSE OF THE OFFICE OF MANAGEMENT AND BUDGET TO WRITTEN QUESTIONS SUBMITTED
BY HON. ALAN CRANSTON, RANKING MINORITY MEMBER OF THE SENATE COMMITTEE ON
VETERANS' AFFAIRS

Question #1

What information do you have with respect to the numbers of new, specially-trained personnel that the V.A. would need, at both the central office and the field station level, to enter into and manage the large-scale contracting operations that A-76 contemplates and with respect to the annual cost of these positions?

Answer:

The costs you refer to are contract administration costs and are considered when calculating the cost to the Government of contracting out.

The cost comparison procedures of Circular A-76 require 4% of the contract price or expected cost to be charged to the cost of contracting-out before it is compared to the cost of in-house operation.

Question #2

What O.M.B. and White House functions such as food services, custodial services, and groundkeeping, are currently carried out by outside contractors?

Answer:

Most of the services of this nature are contracted out or are scheduled for review in accordance with A-76. Food services for the New and Old Executive Office Buildings (where all OMB and most White House staff are housed) are obtained from GSA, which in turn contracts for the services. Custodial and janitorial services for the New Executive Office Building are also obtained from GSA-furnished contractors. Because of Secret Service and White House Security restrictions, custodial and janitorial services for the Old Executive Office Building and the White House are required to be provided by GSA employees.

OMB and the White House obtain automatic data processing (ADP) and audiovisual services from the Office of Administration (OA) within the Executive Office of the President. OA contracts for 90% of the ADP services. The in-house portion and audiovisual services (which OA has identified as a CA) have been scheduled for review in accordance with A-76. The White House Mess is operated by the Department of Defense and is subject to the provisions of Circular A-76 as implemented by DOD.

Question #3

It is my understanding that, as part of the Administration's emphasis on Circular A-76, agencies will be required, beginning with the FY 1983 budget cycle, to reflect in their budget submissions their assumptions about savings that might be achieved through contracting-out. Is this correct?

(If yes) Please explain how this requirement is to be implemented with specific reference to the V.A. and with respect to D.M.& S., how it is to be implemented in terms of section 601(b)(2) of Public Law 97-66?

Answer:

Yes. Section 13.2(1) of OMB Circular A-11, "Preparation and Submissions of Budget Estimates" requires agencies to ensure that budget estimates reflect the probable impact of decisions concerning the mode of performance of commercial and industrial activities made in accordance with OMB Circular No. A-76. The data received from agencies will be used to review agency requests, overall resource allocations, productivity improvements, and prepare a special analysis display on progress toward greater reliance on the private sector. This requirement was implemented with the issuance of OMB Bulletin 81-15 in April, 1981, which required Executive Branch agencies to report to OMB on their progress in implementing the Circular. The VA has not completed their report, so we are unable to determine with any degree of accuracy the impact of full implementation of A-76 in the VA. With respect to implementation of the Circular in the Department of Medicine and Surgery (DM&S), Section 601 (b)(2) of P.L. 97-66 (S.917) prohibits the conduct of A-76 cost studies in DM&S unless funds are specifically appropriated for that purpose. We are very much concerned with the loss of management flexibility as a result of the requirements of this section, because it precludes the VA from determining the most efficient and effective ways to deliver veterans' health care. As the President indicated when he signed S.917, OMB will work with the Congress to allay its concerns about the implementation of OMB Circular A-76 and to find a mutually agreeable approach to the Circular's application.

We firmly believe that the best interests of the VA and the veteran will be served by repealing the impediments to A-76 implementation contained in Section 601 of S.917. Until this Section is repealed, or funds separately allocated for studies, Bulletin 81-15 will not be implemented in the VA's DM&S function.

Question #4

The VA, in its testimony, describes various functions as outside of Circular A-76 coverage. Included in this list of "inherently Governmental functions" are "management of Government programs" and "direction of Federal employees".

Does OMB agree that these are outside of Circular A-76 coverage? (If yes) Does that mean that the type of service provided by another of today's witnesses, Servicemaster Industries, which is described in their testimony as providing "management services to the health care community" and as "managing the hospital's employees" is not the type of service that is encompassed by Circular A-76?

Answer:

If the Government programs the VA refers to in testimony are inherently Governmental, and must be performed by Government employees, then we agree that it should not be contracted out. We want to make it clear that making the determination as to which programs or activities are inherently Governmental, and which are CA's subject to the Circular requires judgement on the part of agency officials who are implementing A-76. The guidelines, provisions and examples of Governmental functions and CA's in A-76 provide an adequate framework to make such judgements.

When "direction of Federal employees" establishes an employee-employer relationship between a contractor and the Government, then the contract is illegal. With respect to the Servicemaster Industries services, such as "management services to the Health Care Community" and "Managing Hospital Employees," we would have to say that these are very general descriptions and open to interpretation. However, "management only" contracts are not authorized by A-76 since this would amount to establishing an employer-employee relationship. We want to point out, however, that Servicemaster Industries does provide complete contract services in the Department of Defense for hospital custodial services, including their critical care areas. Although DOD refers to this program as "Hospital Aseptic Management Services" the contractor fully manages and operates this critical function using contractor employees only.

Question #5

Kenneth Blaylock, National President of the American Federation of Government Employees, indicates in his testimony his view that under Circular A-76, an agency's estimate of the in-house cost of performing a function will be inflated. He cites a number of reasons for this, including the fact that A-76 requires that such estimates be based on current staffing and organizational patterns rather than potentially more efficient patterns; that an agency must add a fixed 21 percent markup over wholesale for goods ordered through GSA, and that estimates of in-house costs must add an arbitrary 20.4 percent for retirement costs. By contrast, Mr. Blaylock states that the contractors' costs are understated because the cost comparisons are based on three-fifths of the actual cost of severance pay, homeowner's assistance, pay rate retention, relocation and retraining expenses, and the physical inventory to implement the contracting out. Would you please comment on these assertions?

Answer:

Mr. Blaylock is incorrect in his assumptions. As it is now written, A-76 is most definitely slanted in favor of retaining CA's in-house. Paragraph 9.c.(1) encourages agencies to reorganize in-house activities for maximum efficiency, when possible, before making a cost comparison with contract performance; the 21 percent add-on to GSA wholesale material prices is the estimated indirect cost to the Government of GSA providing these materials to Government agencies. In most instances, GSA does not pass this cost onto the user agency. Since the Circular requires cost comparisons to be aimed at full cost to the maximum extent practicable in all cases, to ignore this cost would artificially deflate the cost estimate for in-house performance.

All significant Government costs (including indirect costs) must be considered, for both Government and contractor performance (paragraph 9.a.(3)). The 20.4 percent factor to be added for retirement costs was calculated by the Office of Personnel Management, with the concurrence of the General Accounting Office. Again, in order to develop a full cost estimate to the Government of providing the services in-house, retirement costs must be considered, as they also would be by the contractor.

In the second part of the question, Mr. Blaylock states that "contractors' costs are understated because cost comparisons are based on three-fifths of the actual cost to the Government of severance pay, homeowners' assistance ... etc." This statement is incorrect. The cost comparison procedures of A-76 state that if an activity is converted to contract performance, certain labor-related expenses -- severance pay, homeowners' assistance, pay rate retention, relocation and retraining expenses -- will be incurred. The amount of these expenses are not fixed at any amount, but rather estimated in consultation with management and the personnel department. These costs are charged to the cost of contracting-out before it is compared to the cost of in-house operation.

Question #6

Elsewhere in his testimony, Mr. Blaylock states that "once a contract has been awarded to a small business concern, A-76 provides for conversion to in-house performance." What is the reason for this limitation?

Answer:

Mr. Blaylock's statement is incorrect. Paragraph 10.e. (2) of A-76 states that "contracts awarded under authorized set-aside programs will not be reviewed for possible in-house performance. Additionally, new requirements which would be suitable for award under a set-aside program should be satisfied by such a contract without a comparative cost analysis." On the other hand, paragraph 10.e. (3) states that activities in excess of \$100,000 annually "will not be considered for performance under a set-aside contract except when the conversion is justified by a comparative cost analysis."

Question #7

In its testimony prepared for today's hearing, the V.F.W. express some significant concerns about the ultimate effect of the VA contracting-out all ability to perform a particular function to an outside contractor. In this regard, the V.F.W. quotes from a statement made to the House Committee on Veterans' Affairs last month by the president of a company that manufactures and sells housekeeping products to hospitals and other institutions. In his testimony to the House, that witness stated that, in his view, "Surrendering all VA supervisory and housekeeping personnel into the direct employment of the contractor is frightening. The threat of the then current contractor's removal of all its' housekeeping employees means the VA would have to accept virtually any terms offered. Each contract renewal would be tantamount to a strike."

How do you believe that the VA can protect itself from just such a situation?

Answer:

The V.F.W. witness apparently assumes that there is only one contractor capable of providing janitorial services to the VA, and therefore would place the Government in a most unfavorable position at contract negotiations. This assumption, of course, is incorrect. The District of Columbia Yellow Pages currently lists 121 janitorial service firms, many of whom would probably be capable of providing the needed services to the VA. Further, the success of DoD's hospital custodial services contract program refutes the witnesses contention.

When the threat of strikes is perceived to be a problem, it is entirely appropriate for the Government to require the contractor to include a strike contingency plan in the contract. This plan would set forth what actions the contractor would take to effectively mitigate the effects of and to ensure continuity of services should a strike occur. We have no evidence that would support the contention that strikes by contractor employees has affected the delivery of services to a significant extent.

Question #8

Within the Department of Defense, and especially within the U.S. Air Force, how many A-76 service contractors have been declared in default? In which of these situations was it necessary to return the function to in-house performance?

Answer:

The Department of Defense keeps no formal statistics on the incidence of default in contracts resulting from Circular A-76 conversions. However, to DoD's knowledge, only a very small number occurred, and when default did happen, contingency planning precluded any loss of service.

Question #9

How many DoD A-76 contracts have required intra-agreement renegotiation of payments in the past five years? What is the total dollar value of those renegotiations versus the total dollars of the original bids accepted?

Answer:

The DoD does not maintain these statistics. However, the Defense Audit Service, in a recent study, addressed the question of cost growth in service contracts. This study concluded that based on their review, there was no evidence of contractor buy-ins nor unusual cost growth. A copy of the study is attached.

Question #10

I understand that one problem for Governmental agencies in attempting to be competitive with private contractors is the Federal blue collar wage rates and the manner in which they are computed. What steps, if any, has OMB taken in the last 10 years with DOL and OPM to remedy the existing imbalance and what has been the result of those steps?

Answer:

The level of the wages determined by the blue collar pay setting system has been of concern to the Executive Branch since the early 1970's. Based on OPM and GAO studies of 1973 and 1974, the President's Panel on Federal Compensation recommended significant reforms in that system (Rockefeller Report). These reforms were first proposed to the Congress by President Ford in 1975 and each President since has included them in his legislative program (S.1340 and H.R. 4477 of this Congress). However, the Congress has not taken action to enact the necessary legislation.

Question 11:

If a VA hospital were to contract for food preparation and laundry services, it would seem to me desirable that the contractors be required to perform those services using the hospital's kitchen and laundry facilities. The reason for such a requirement would be that, in the event of an interruption in a contractor's performance, the services could most readily be reinstituted without the delays that would otherwise be involved in getting the kitchen or laundry back into functional operation. Do you believe that including such a requirement in the contracts would be permissible and justified?

Answer:

Such an arrangement between the contractor and the Government is permissible and has been carried out successfully in many instances. The Cost Comparison Handbook permits the solicitation of bids using Government facilities if it is in the best interest of the Government. Such decisions are left up to agency management.



DEFENSE AUDIT SERVICE
1300 WILSON BOULEVARD
ARLINGTON, VIRGINIA 22209

REPORT
NO. 80-105

May 27, 1980

MEMORANDUM FOR DEPUTY ASSISTANT SECRETARY OF DEFENSE (SUPPLY,
MAINTENANCE AND TRANSPORTATION)

SUBJECT: Review of Commercial or Industrial Type Activities
Converted to Contract in FY 1977 (Project OSI-032)

We have completed our review of Commercial or Industrial Type Activities (CITA) converted to contract in FY 1977. The objectives of the review were to determine the extent of cost growth on in-house CITA operations converted to contract in FY 1977 and to determine the reasons for abnormal cost increases.

We identified 39 CITA functions at 30 military installations that were converted to contract in FY 1977. Since that time, cost growths for 20 of the functions at 18 installations exceeded the annual inflation rate for at least 1 year.

We examined 10 of the 20 CITA functions with cost growths greater than the annual inflation rate. For 8 of the 10, we found that the increases were primarily attributable to significant additions to the scope of work required. For example, the total cost of custodial contracts at the Naval Public Works Center, Great Lakes, Illinois, increased by 335 percent between FY 1977 and FY 1980. Annual cost increases ranged from 23 to 180 percent. We found that the cost increases were due primarily to increased work requirements. The actual square footage covered by the custodial contracts increased by 384 percent between FY 1977 and FY 1980. Consequently, the actual cost per unit of work did not increase.

The 2 cases where cost increases were not related to increased work requirements involved food service operations at Holloman Air Force Base and at Fort Benjamin Harrison.

At Holloman Air Force Base, the contract price increased about 145 percent and the cost per meal served (a guide for evaluating food service attendant contracts) increased 51 percent between FY 1977 and FY 1978. The apparent reason for the sharp increase was an erroneous "under bid" by the contractor. Within a few weeks after the contractor commenced performance, he claimed he was "misled" by the manning chart contained in the Air Force solicitation and as a result significantly underestimated his bid.

The bid solicitation included a manning chart that showed the suggested number of mess attendants needed by half-hour increments to accomplish the work. This chart was furnished as a guide only. Holloman AFB, the Tactical Air Command and the Air Force Logistics Command disagreed with the contractor's claim and disallowed it. The Air Force Contract Adjustment Board, however, overruled this decision and ultimately directed Holloman AFB to pay the contractor an additional \$85,296. This amount, when added to the original contract price, may have exceeded the cost to keep the function in-house. Since this was a specific set-aside contract, it no longer falls under the CITA program requirements for periodic follow-up review. Consequently, the contractor with satisfactory performance is almost guaranteed the future work even though his costs may exceed the costs to perform the function in-house.

The food service contract cost at Fort Benjamin Harrison increased 25 percent between FY 1978 and FY 1979. The reason cited for the price increase was the inclusion of minimum staffing requirements in the succeeding FY 1979 contract. The contracting officer included the minimum staffing requirement because the contractor had frequently submitted invoices and was paid for work that he claimed was over and above the original contract requirements. In our opinion, the contractor's claims that the work he performed was over and above the original contract requirements were questionable. For example, the bid solicitation required complete sweeping, cleaning and mopping. The solicitation also noted that the dishwashing equipment had a history of rather frequent mechanical breakdowns. The contractor should have considered the implications of these conditions in his bid. However, when the dishwasher broke, he invoiced for additional labor to move the dishes to the alternate dishwasher and for labor to clean up the water from the inoperative dishwasher. The contractor was obligated to report inoperative equipment to the post engineers; however, we were unable to identify any work orders where the contractor requested the equipment be fixed.

Based on our review, it does not appear that contractors of CITA functions are bidding low and then unrealistically raising their prices on subsequent contracts.

Edward R. Jones
Acting Associate Director
Systems & Logistics Audits

Senator CRANSTON. In light of the provisions of section 602(b)(2) of Public Law 97-66, which preclude the VA from spending any funds that have been appropriated for medical care purposes to conduct contracting out studies, does OMB intend to request a separate appropriation to fund some or all of the studies that OMB believes the VA should now be conducting?

Mr. SOWLE. To my knowledge at this point there is no plan to do that.

Senator CRANSTON. How will the costs of any future studies be covered, then?

Mr. SOWLE. In these particular areas covered by 601, there will be no activity in that area unless we can talk to this committee and members of the VA to see if we can't come up with some acceptable plan for the VA to make use of the contracting process.

Senator CRANSTON. The VA's testimony today states that OMB accepts the VA General Counsel's opinion of March 21, 1980, that Circular A-76 cannot legally be applied to the basic medical operations of DM&S.

Shouldn't the question as to what constitutes basic medical care operations ultimately be entrusted to the VA's Chief Medical Director, the official charged by statute for the operations of the Department?

Mr. SOWLE. Sir, we believe at this point that the head of the agency can make that determination in coordination with the Chief Medical Officer.

Senator CRANSTON. How does OMB answer concerns about the effects of strikes or other work actions by A-76 contractors, employees, on the VA's ability to provide quality health care?

Mr. SOWLE. Senator Cranston, as I mentioned in my longer statement, there are provisions that can be made for strike contingencies. These have worked out well in the past when strike contingency plans have been put into effect. Generally a lack of experienced personnel has not been experienced during strikes because of the planning that was done ahead of time.

Senator CRANSTON. In the case of the Air Force hospitals, how was the cleaning work done when interruptions occurred?

Mr. SOWLE. I'd like to defer that question to the representative from the Department of Defense who is here, but it's my understanding that the main elements of that were use of supervisory people, and the contractor brought in additional people to temporarily perform the work.

Senator CRANSTON. Were uniformed personnel brought in?

Mr. SOWLE. Sir?

Senator CRANSTON. Were uniformed personnel brought in?

Mr. SOWLE. I'm not sure of that. I don't know.

Senator CRANSTON. After a contract has been awarded and the VA employees concerned are gone, how are essential functions that need to get done on a daily basis—like food services, laundry and cleaning—really done if the contract's performance is interrupted by bankruptcy or some other cause?

Mr. SOWLE. Well, sir, I know of one case where there was a bankruptcy and the service continued just as before, with the employees of the contractor continuing to work on the jobs that they performed prior to the bankruptcy.

This again would be an element that would be included in the contingency plan.

Senator CRANSTON. When a comparison is being made between a particular service being performed in-house or on a contract basis, does Circular A-76 require an assumption that both sources of the service would do a similarly competent job, or does it permit an assessment of the likelihood of such comparability?

Mr. SOWLE. Well, in some cases, depending upon the work statement, there could be a higher level of performance required of the contractor than might currently exist with the in-house operation.

However, for cost comparison purposes, and as a part of the contracting process, the use of preaward surveys and evaluations of contractors' proposals are techniques that are normally used to insure the potential contractor fully understands the work contemplated and has the necessary financial and technical ability to deliver satisfactory work in the event of an award.

Senator CRANSTON. In the event that a particular service is shifted to a contract basis, is the contractor under the circular required to offer to hire all VA workers displaced by the contract to the full extent of the size of the contract work force, or is the circular requirement only that, to the extent that the contractor has openings, displaced employees must be given an opportunity to fill those positions?

Mr. SOWLE. Well, I think it's not only openings but the people have to be qualified, and assuming that they're performing the same function as the contractor would require, there's an assumption that they are qualified.

So those factors are considered, but not in exactly the light in which you present them, Senator.

Senator CRANSTON. Which OMB and White House functions, such as food services, custodial services and groundkeeping, are currently carried out by outside contractors?

Mr. SOWLE. I think many of the services at the White House and OMB are contracted out.

I can't tell you specifically about every service.

Senator CRANSTON. Would you give us a detailed statement for the record on that, and what's proposed?

Mr. SOWLE. Yes.

[Subsequently, the Office of Management and Budget submitted the following information:]

COMMERCIAL ACTIVITIES OBTAINED BY CONTRACT IN THE EXECUTIVE OFFICE OF THE PRESIDENT

The White House Mess is operated by the Department of Defense and is subject to the provisions of Circular A-76 as implemented by DOD. OMB and the White House obtain audiovisual products and services from the Office of Administration (OA) in the Executive Office of the President. OA has identified this as a commercial and industrial activity (CA) and has scheduled it for review. OMB and the White House also obtain automatic data processing (ADP) services from OA. OA contracts for 90 percent of the ADP services, and has scheduled the inhouse portion for review. Custodial and janitorial services are obtained from GSA, which contracts for the services.

Groundkeeping is obtained from GSA (Executive Office Buildings) and the Park Service (White House only). GSA and the Park Service are in the process of inventorying their CA's and once inventoried, will schedule them for review in accordance with A-76.

Senator CRANSTON. A recent GAO report entitled "Pension Losses of Contractor Employees at Federal Installations Can Be Reduced" raised some serious concerns about the extent to which employees of contractors providing services to the Federal Government lose pension benefits because of a frequent change in their employers, as different contractors receive the service contracts, even though the employees don't change jobs.

Are you satisfied that adequate steps are being taken at the present to reduce that problem?

Mr. SOWLE. Senator, I am personally not familiar, nor do I have any data as to that problem. I think we would have to work with the various agencies and departments to make that sort of—

Senator CRANSTON. Well, would you talk to the Labor Department about that and give us something for the record?

Mr. SOWLE. Yes.

[Subsequently, the Office of Management and Budget submitted the following information:]

MAJOR ELEMENTS IN THE A-76 COST COMPARISON PROCESS, INCLUDING THE SERVICE CONTRACT ACT WAGE RATE DETERMINATION

See overview of the A-76 cost study procedures.

The Service Contract Act requires contractors to pay service employees at least the wage and fringe benefits prevailing for similar work in the locality where the work is being performed. These wage and fringe benefits are determined by the Department of Labor with due consideration given to federal wages and fringe benefits paid to Government service employees.

All service contracts awarded as a result of a cost comparison study are required to include a clause stating that the contractor will abide by the provisions of the Service Contract Act and pay his employees the wages and fringe benefits set by the Department of Labor

OMB'S POSITION ON THE STATUTORY DOD REQUIREMENT THAT ORGANIZATIONS UNDERGOING COST STUDIES BE ORGANIZED IN "THE MOST EFFICIENT AND COST EFFECTIVE ORGANIZATION"

OMB Circular No. A-76 already requires agencies to assure Government operations are organized and staffed for the most efficient performance by preceding A-76 reviews with internal management reviews and reorganizations for accomplishing the work more efficiently (paragraph 9.c.(1)). This is an administrative requirement more effectively managed by regulation within the executive branch. Therefore, we believe a statutory requirement is neither necessary nor appropriate.

Enclosed is OMB's July 20, 1981 response to the GAO report "Pension Losses of Contractor Employees at Federal Installations Can Be Reduced."

Overview of A-76 Cost Study Procedures

Common ground rules.

- Both contractor and in-house cost estimate must be based on same statement of work (SOW) and level of performance.
- SCW should be performance oriented and include written performance standards.
- Standard cost factors in Cost Comparison Handbook will be used.
- Cost comparisons will use full costing to maximum extent possible.
- Both contractor and in-house comparative cost analysis are normally evaluated for a performance period of three years.
- Solicitation should provide for two prepriced options to guard against "buy-ins".

Calculating cost of Government operation.

- The in-house estimate is developed based on the requirements in the SOW.
- The estimate normally includes direct labor, material overhead, fringe benefits, overhead, G&A, and other miscellaneous costs such as one-time conversion costs.
- There are three standard cost factors prescribed:
 - Retirement factor of 20.4 percent which is based on a dynamic normal cost projection for civil service retirement fund.
 - Life and health insurance factor of 3.7 percent which is based on actual cost.
 - Workman's compensation, bonuses, and awards factor of 1.9 percent which is based on actual cost.
- Existing in-house activities will not be converted to contract unless it will result in a savings of at least 10 percent in estimated Government personnel-related costs.
 - Favors continuing status quo.
 - Bogie included to prevent "flip-flop" and provide for conversions only when savings are significant.

Calculating cost of contract operation.

- Contractor's proposal is developed based on requirement in SOW.

- The following costs are generally added to contractor's proposal: transportation, contract administration, and other costs where applicable such as GFP, standby maintenance, etc.
- The contract administration cost factor is four percent of the contract price. This is a standard factor that must be used and is derived from DLA's experience in administering major weapons systems contracts.
- When the function being cost studied is a "new start" (i.e., not an existing in-house activity), there must be a savings compared to contract performance of at least 10 percent in Government personnel-related costs plus 25 percent of cost of ownership of equipment and facilities before function could be brought "in-house".

Other provisions.

- Independent audit required by Circular of cost comparison to ensure it is current, accurate, and complete.
- Each agency must establish formal appeals procedure to resolve questions of in-house/contract decision.
- All affected parties given 5 - 15 days to appeal decision based on data in cost comparison.
- All appeals must be resolved in 30 days by official at same or higher level than official who performed cost study.
- Not subject to negotiation or arbitration with affected parties.
- Agency decisions are final, although if a contractor protest is filed with GAO, they have determined they can rule on cost comparison because it "affects integrity of bid system."

Implementation.

- Agencies required to fully implement Circular including conducting all cost studies by March 1982.
- Have extended implementation date to September 1982 for majority of agencies except for (DOD, VA, HUD). They have been granted additional extension due to size of inventory.

JULY 20, 1981.

WILLIAM J. ANDERSON,
*Director, General Government Division, U.S. General Accounting Office, Washington,
 D.C.*

DEAR MR. ANDERSON: This is in response to a GAO draft report entitled "Pension Benefit Losses of Contractors' Employees Working at Federal Installations Can Be Reduced" which was furnished to OMB for comment prior to final issuance.

The draft report suggests that it may be desirable to protect pension rights of employees of Government contractors in situations where the Government decides to change contractors and employees of the old contractor continue on under the new contractor. The report recommends that if the Congress decides to adopt such a policy, it place implementing responsibility in the Office of Federal Procurement Policy.

We recommend that the report make clear that pension benefits of contractor employees are a responsibility of the contractor. They are not now, and never should be, a responsibility of the Government in its role as a party to a contract. Accordingly, any policy the Congress considers should carefully protect the Government against claims from contractor employees for unpaid or disregarded pension rights. Such claims should be between the contractor and his employees with employee rights protected by the Employee Retirement Income Security Act and other laws.

Further, the draft report notes that the Department of Labor has determined that regulations dealing only with work on Government contracts would not be a feasible solution because (1) the pension portability and vesting problems of the Government contract employees studied did not appear significantly different from those of similar employees in the general population and (2) the employees went back and forth between government contract work and private work. This appears to us to raise a serious question, yet the draft report contains no recommendation with respect to overcoming the problems.

If the Congress were to determine that the pension benefits at Federal installations should be protected, OFPP could establish a Government-wide policy and implementing procurement regulations to help ensure such protection.

Thank you for the opportunity to review the draft report. We look forward to receiving the final report.

Sincerely,

EDWIN L. HARPER,
Deputy Director.

Senator CRANSTON. Does Circular A-76 cost comparison contain any element that would factor in the future cost to the Government in income transfer or other support programs of significant numbers of contractor employees retiring without any pension plan coverage?

Mr. SOWLE. Again, I don't believe that—I would ask Ms. Druyun if she is aware, but I don't believe that has been fully explored.

Senator CRANSTON. Shouldn't that be factored in?

Mr. SOWLE. Has it been factored in, I guess that's the—

Senator CRANSTON. If it hasn't been, shouldn't it be?

Mr. SOWLE. Transfer payments? I would think that would appear to be a reasonable thing, however, I need further time to examine the issue.

Senator CRANSTON. Would you let us know back what you've done on that?

Ken Blaylock, the national president of the AFGE, in his testimony for today's hearing, noted that the cost comparison developed in DOD, in conjunction with the Circular A-76 process, must be based on, "the most efficient and cost-effective organization" of the function to be contracted out.

Mr. Blaylock then states that the OMB adamantly opposed this requirement.

What is your current evaluation of the statutory approach, and would you support such a limitation being enacted with reference to contracting out in the VA?

Mr. SOWLE. I would like—that's kind of a long, involved question, Senator. I'd really like to have an opportunity to look at that one.

Senator CRANSTON. That completes my questions. I'll have further in writing.

Chairman Simpson has something he wishes to submit in writing.

We're now going to have to recess briefly until Senator Simpson returns, because I have to go to a Defense procurement matter.

Thank you very much. It will be a brief recess, I trust.

Mr. SOWLE. Are we excused, Senator?

Senator CRANSTON. Yes.

Mr. SOWLE. Thank you.

Senator CRANSTON. Thank you.

[Whereupon, a brief recess was taken.]

[Hearing resumed.]

Chairman SIMPSON [presiding]. Come to order. Col. Paul McNally.

TESTIMONY OF COL. PAUL McNALLY, CHIEF, MEDICAL LOGISTICS DIVISION, AIR FORCE MEDICAL SERVICES CENTER

Col. McNALLY. Thank you, Mr. Chairman.

This is Col. Fred Ordman, my colleague who has had extensive experience with the Air Force Medical Service in contracting.

It is a pleasure and a privilege to be here today to discuss the Air Force experience with contracting for housekeeping services in medical treatment facilities. In 1973, the Secretary of the Air Force directed that all Air Force custodial service be evaluated for potential conversion to contract operations. After deliberation, the Air Force Medical Service decided that contracting for housekeeping services in medical treatment facilities could provide the necessary services for mission accomplishment.

The statement of work which ultimately evolved is now the cornerstone upon which all Air Force medical treatment facilities, housekeeping contracts are built.

Supporting this cornerstone is the compelling essentiality of agency commitment to a specifically structured procurement process which assures contracting with technically competent contractors. Until this procurement process was established Air Force resistance to contracting resulting from historic dissatisfaction with contractors secured under restrictive procurement modalities could not be overcome. The statement of work requires a comprehensive asepsis management program to insure a pathogenic free environment. The scope of service encompasses responsibility for hospital housekeeping in all areas of the hospital, including critical care areas such as surgery, delivery room, intensive care, and coronary care units. The contractor provides these services through a qualified work force and technically oriented management structure to direct the operation.

When we prepared the initial statement of work we believed that the critical element in achieving a satisfactory level of performance

was a contractor's experience level and quality of management. As a consequence, a substantial portion of our standards relate directly to the contractor's management capability coupled with requirements for routine accomplishment of housekeeping tasks. We believe the quality of service is crucial. Through our contracting program we have maintained a high level of quality consistent with contractual requirements.

We are able to obtain cost effective and quality service for two basic reasons. The first relates to our method of evaluation of the contractors' proposals. Each contractor's proposal in such areas as the management system, management support structure, labor-management relations, staffing plans, training programs, quality control procedures, and ability to achieve an orderly phase-in of services are critically reviewed. We also carefully review the contractor's proposal to insure that the services proposed by the contractor will enable our facilities to achieve the infection control standards of the Joint Commission on Accreditation of Hospitals.

The second factor in achieving a satisfactory level of performance relates to the structuring of our contracts. We use performance oriented specifications and include a collateral Government quality assurance plan. The implementation and operation of a quality assurance plan establishes a sound and enforceable basis for contract administration.

The method just described is known as a hospital aseptic management system or HAMS. Contractor performance under this program has been good, not only from an esthetic standpoint, but also from the perspective of maintaining a clean and safe environment. Although we have experienced some problems, the provision of health care to DOD beneficiaries has not been adversely affected. To date, two locations were impacted when a contractor declared bankruptcy and a contract dispute resulted in termination of services at one other location. In each instance reprourement of services was effected expeditiously.

The cost efficiency of continued contract operations is insured through strict adherence to the review procedures in OMB Circular A-76. As of June 30, 1981, the approximate annual dollar value of HAMS contracts at 36 locations was \$14 million.

The Air Force considers these contracts to be a cost-effective alternative to performing the required service in-house. Although this testimony has principally focused on housekeeping services, we also contract for laundry services at all but four bases in the States. In addition, we have a new initiative currently under formal solicitation for complete real property maintenance contracts at five hospital locations.

I will be glad to respond to your questions, sir.

Chairman SIMPSON. Thank you very much, Colonel. Could you specify exactly what services at Air Force hospitals have been contracted out under compulsion of A-76 and how much money is involved in contracts for each said service, and then tell us if there are other contracting activities relating to commercial and industrial activities within the Air Force hospital system?

Colonel McNALLY. The Air Force has contracted for an extensive period of time for both laundry and housekeeping services. Historically most of our service contracting was not forced by A-76. We

did use the provisions of A-76 to determine project cost effectiveness.

There have been only several locations in recent years that have been contracted as a result of conformance with A-76 implementation. Our most recent case is the Hill Air Force Base Hospital. Under the A-76 direction at Hill we achieved an inhouse cost of \$690,000, for a 3-year period, and a contractor cost of \$454,000 for that same period. That facility did go out under contract and realized a net savings of \$236,000 over the life of the contract.

Chairman SIMPSON. What has been your experience with regard to food service? Have you dabbled in that particular line?

Colonel McNALLY. The line of the Air Force has contracted considerably in that area, but the medical service has not. We have done several things to reduce our staffing, and that is in our smaller facilities. We satellite online facilities and transport the food from the line dining facilities in insulated containers to our patients. In addition, we have used preprepared meals to reduce hospital food production staffing.

Chairman SIMPSON. What percentage of displaced Air Force hospital employees were subsequently rehired by the contractor? I think that is something the committee is interested in. I would appreciate any similar information you might have with regard to employees that were hired under veterans preference priorities. Can you give us any information on that?

Colonel McNALLY. To the extent that the record will permit, we can provide that information to you, although the civil service office on the Air Force bases have a very aggressive program to retrain and to relocate displaced employees. I am personally not aware of anyone who has wanted to remain and has been unable to stay within the civil service system through an attrition process.

[Subsequently, Colonel McNally submitted the following information:]

Hill and Keesler AFB hospitals are the facilities that have recently converted to using the A-76 method of cost comparison. At Hill all of the Government employees were reassigned to jobs elsewhere on base. None were available for the contractor to hire. At Kessler the contractor hired 9 civil service employees at the start of the contract, only one of these is still employed by the contractor. No information is available about veterans preference hiring.

Chairman SIMPSON. Are you aware of how many have gone with the contractor, with the suppliers?

Colonel McNALLY. There are some that have done that. We would have to provide that information for those bases where historic records are available.

[As of the date of publication of this hearing record (June 1982), Colonel McNally has submitted no response to this question.]

Chairman SIMPSON. I think we had figures that there was a rehire rate of 60 percent or something like that, or much higher, 90 percent in some cases; when the contracting was formed, the supplier would hire up to 60 or 90 percent of those who had been displaced by the—

Colonel McNALLY. Your figure of 90 percent equates to my experience of what happens when one contractor leaves and a new contractor comes in. The retention of the civil service employee is much greater in the system than that.

Chairman SIMPSON. I would appreciate it if you would also, since you are providing other material into the record, that you provide us with detailed information regarding the laundry and housekeeping contracts, because that after all is one of the specific things we are talking about contracting out under A-76 and the studies with the various centers. You might set forth the facility involved, the duration of the contract relationship, the amount of money involved, savings realized in each contract, and if terminated, the reasons for termination. That would be very helpful to the committee.

Colonel McNALLY. Yes, sir.

[Subsequently, Colonel McNally submitted the following information:]

The only detailed information available is for Hill and Keesler AFB hospitals. This data was previously provided by OFPP. The other facility conversions were early-to-mid 70's and the data is no longer available. Also present criteria for conversion is different from that previously used. All Air Force hospitals in the continental U.S. are presently under contract for hospital housekeeping services. By Air Force Policy, these contracts are subject to an informal cost review. This review assures we are getting at least a 10-percent savings of personnel costs plus 25 percent of capital investment costs. Except for one incident, the only contracts that have been terminated were due to bankruptcy of the company. At these facilities the contractor's employees were hired as temporary civil service employees, equipment was rented and the contracting offices performed procurement. There was no loss of service to the facility.

Chairman SIMPSON. I would also appreciate it if you could provide us with similar information on the Air Force's experience with contracting out all types of services, not just hospital services. That would be helpful. That, of course, need not be broken down into individual facilities, but just summaries of other categories that I have referred to.

Colonel McNALLY. As I mentioned, we have contractors for both housekeeping and laundry service for many years. We will provide that information to the extent the records are available.

[As of the date of publication of this hearing record (June 1982), Colonel McNally has submitted no response to this question.]

Chairman SIMPSON. I thank you very much. We appreciate your testimony. Other members of the committee may have written questions. I will have a few more. Thank you for being with us. I appreciate it.

[The response of Colonel McNally to a written question submitted by Hon. Alan Simpson, chairman of the Senate Veterans' Affairs Committee, follows:]

Senator SIMPSON. With respect to the laundry services contracted out, how many of these contracts were negotiated under compulsion of A-76 and how many predated the implementation of A-76? Of those that pre-dated A-76, were any motivated by cost factors alone?

ANSWER. We converted the majority of our laundry services in the early and mid 70's. The criteria used for the cost comparisons at that time were different from the present requirements. However, the cost comparison criteria used assured the conversion was cost effective.

[The following written questions were submitted to Colonel McNally shortly after the hearing, and despite repeated subsequent efforts by the Committee staff to obtain responses, none have been furnished to the Committee as of the date of publication of this hearing record:]

Senator SIMPSON. (1) With regard to the implementation of section 502 of Public Law 96-342, has that provision's requirement that a government cost estimate be based on an estimate of the "most efficient and cost-effective organization" of the function under review actually resulted in reorganization of any of the departments under review? What effect, if any, has this provision had on Air Force contract policy and on the five upcoming contracts for real property maintenance services?

(2) The GAO report on DOD contracting activities, PLRD-81-19, discusses the contract for custodial services at the Air Force Academy. The report indicates that due to an incomplete statement of work, the 3-year cost-savings associated with the contract were actually \$708,000 (18 percent of the total contract price), less than projected. Why was this incomplete statement of work not corrected before the contract was entered into? What, if any, additional safeguards now exist to prevent a recurrence of this problem? Why was the in-house cost estimate based on the existing in-house operation rather than the same statement of work used by the contractor, or on the "most efficient and cost-effective organization", as required under Public Law 96-342? What would the in-house estimate have been if it had been based on the same statement of work used by the contractor?

Senator CRANSTON. (1) What generally is the background, experience, and grade level of the Air Force contracting officers who prepare, award, and manage the contracts described in your statement?

(2)(A) Are the other uniformed services, to your knowledge, following the lead of the Air Force in contracting for housekeeping services in medical treatment facilities?

(B) [If not] What not?

[If yes] Could you please obtain, for the record, statements of what each is doing?

(3) In your statement, you note that "the contractor provides these services through a qualified work force". Is that work force comprised of Government employees who are supervised by the contractor or is it comprised of contractor employees?

(4) On page 3 of your statement, you state that you have experienced some problems with contractors.

(A) Have there been problems other than those noted in the statement where the contractors declared bankruptcy or the services were terminated following a contract dispute?

(B) With reference to the examples cited in your statement, you note that "reprocurement of services was effected expeditiously". Was there any break in the performance of cleaning services by outside contractors at the facilities involved?

[If yes] How long were those breaks and how were the facilities cleaned during those periods?

(5) You mention that as of June 30, 1981, the "annual dollar value of HAMS contracts at 36 locations was \$14 million".

(A) Were there any Air Force health treatment facilities that did not have active "HAMS" contracts at that time?

(B) What do you estimate are the annual savings associated with these 36 contracts as compared to doing the work in-house?

(C) Please submit a detailed estimate of those savings for the record. When that estimate is received, I will submit it to GAO for analysis and comment for the record of this hearing.

(6)(A) Of the Air Force's contracting out experience for food services, how many contracts have been for base food service? How many for hospital food service?

(B) How many food service contractors have been in default of their contract?

(C) In cases involving default, how much money has the Air Force recovered from defaulting contractors?

(7) I understand that, in at least one instance, a DOD facility contracted with a food service contractor despite the fact that an outbreak of botulism has been associated with prior efforts by this contractor. Please describe the quality controls associated with your A-76 process that should prevent such a contract from being entered into and please explain, if you know, how this contract was awarded despite such controls.

(8) In testimony before the House Committee on Veterans' Affairs on October 20, 1981, an OMB witness testified that DOD had between 5 and 20 bidders for each A-76 food service contract.

(A) Were these figures for all food service contracts or is there a difference between the number of bidders for base food service and for hospitals food service contracts?

(B) Broken down as between the two types of food services, how many of the bidders were determined to be responsive and responsible?

(C) How many of these bidders were only interested in a contract for the management of food service?

(9) I understand that Kincheloe AFB in Michigan had a base food service contract and that the contractor went broke and did not pay the employees. I understand further that the employees then stole cooking utensils as their "payment".

(A) What are the details of this contract?

(B) What did it cost to rebuild the food service in terms of equipment and utensils?

(C) What was the cost of reletting this contract?

(D) How much of these costs was recovered from the defaulting contractor?

Chairman SIMPSON. Next is Mr. Robert Gilroy, please, Senior Associate Director of Procurement, Logistics and Readiness Division of the GAO. You might introduce your colleagues.

TESTIMONY OF ROBERT M. GILROY, SENIOR ASSOCIATE DIRECTOR, PROCUREMENT, LOGISTICS AND READINESS DIVISION, GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY GEORGE PECK, HUMAN RESOURCES DIVISION; AND WARREN NAGEL, PROCUREMENT, LOGISTICS AND READINESS DIVISION

Mr. GILROY. Mr. Chairman, on my right is George Peck who is in charge of our work at the Veterans' Administration, and on my left is Warren Nagel who is our area manager for A-76.

With your permission, I will quickly summarize our complete statement which has been entered into the record.

Chairman SIMPSON. Thank you.

Mr. GILROY. We are here at your request to assist you in your oversight review of Office of Management and Budget [OMB] Circular A-76. It is our understanding that the committee is particularly interested in the cost of its implementation versus potential cost savings within the Veterans' Administration's [VA] Department of Medicine and Surgery and the effect contracting out will have on the provision of medical care by VA. Because GAO has not done any reviews which address these issues, the committee has requested GAO to respond to two related areas of interest.

First, you desire information which provides the historical perspective on Circular A-76. And second, you have asked that we cite examples of the types of reviews we have made concerning the implementation of the circular, and the results of these reviews.

Government competition with private enterprise has long been a controversial issue. For over 40 years, congressional committees have made many studies of the extent to which the Federal Government has competed with private enterprise in commercial or industrial activities.

President Eisenhower's budget message of January 21, 1954, was apparently the first public statement of executive branch policy on Government competition with private enterprise.

In January 1955 after months of study, the Bureau of the Budget—the predecessor of OMB—initiated a program to curtail some of the Federal Government's commercial or industrial activities. The policy of the executive branch subsequently evolved through four directives—three bulletins and one circular. The Circular A-76, with five transmittal memorandums, constitute current guidance on contracting out commercial and industrial type activities.

The effect of transmittal memorandums Nos. 4 and 5 issued in March 1979 and September 1980, respectively, is to establish a

three-part statement of basic philosophy: (1) Government reliance on the private sector is a valid principle; (2) certain functions are inherently governmental in nature and must be performed in-house, and (3) the taxpayer is entitled to economy in Government and cost comparisons are appropriate as criteria. Other major changes made in 1979 include a definition of governmental functions, a listing of Government commercial or industrial activities that normally should be contracted, and a narrowing of the criteria for exceptions to the policy. Further, it generally requires that agencies make cost comparisons to support contracting-out decisions and that the savings through contracting should represent at least 10 percent of the estimated Government personnel costs.

Basically, our more recent reviews have involved evaluations of either the propriety of a specific contracting-out decision at a given location or a more comprehensive review of an agencywide or Government-wide nature, possibly involving several types of commercial or industrial activity. Our work in the first category is almost exclusively the result of constituency requests from individual Members of the Congress and generally involve a detailed evaluation of an agency-prepared cost comparison.

For example, in our reviews of specific contracting-out decisions, we found in one review two substantially higher savings by contracting out primarily because the Air Force had understated the number of inhouse employees needed.

In another review we estimated a reduced savings by contracting out because the Army overstated the number of cooks needed in dining facilities.

In another review we estimated that it was more economical to keep the function inhouse. The Army did not agree with our overall conclusion, but it did agree that it had erred in its contracting procedures and agreed to make a new cost comparison.

In our reviews of broad issues surrounding the A-76 program or reviews of major functions of a commercial or industrial nature, we found in a review of 12 conversions that the major reason for contracting out was that the contractor costs were lower than inhouse costs.

In a review of 18 conversions, we found that most of the conversions did not result in performance shortfalls, but we found unsatisfactory performance was experienced in five cases and one conversion was based on an incomplete statement of work. In those cases where contract price increases occurred, they generally seemed to be justified.

In closing we would like to say that although its implementing guidelines could be strengthened, GAO supports the general policy precepts set forth by Circular A-76.

In 1978, we recommended, as did the Commission on Government Procurement in 1972, that the Congress establish a national policy relating to reliance by the Federal Government on the private sector to provide needed goods and services. Without a firm national policy, the future of the A-76 program will be a repetition of the past--confusion, controversy, and ineffective implementation. The policy must be stable and must appropriately balance many issues of national significance. It needs both legislative and executive branch endorsement and support.

I will be happy to respond to any questions.

Chairman SIMPSON. Thank you very much for very helpful information.

[The prepared statement of Robert M. Gilroy, Senior Associate Director, Procurement, Logistics and Readiness Division, General Accounting Office, and the response of the General Accounting Office to written questions submitted by Hon. Alan Cranston, ranking minority member of the Senate Committee on Veterans' Affairs, follow:]

PREPARED STATEMENT OF ROBERT M. GILROY, SENIOR ASSOCIATE DIRECTOR, PROCUREMENT,
LOGISTICS AND READINESS DIVISION, GENERAL ACCOUNTING OFFICE

Mr. Chairman and Members of the Committee:

We are here at your request to assist you in your oversight review of Office of Management and Budget (OMB) Circular A-76. It is our understanding that the Committee is particularly interested in the cost of its implementation versus potential cost savings within the Veterans Administration's (VA) Department of Medicine and Surgery and the effect contracting out will have on the provision of medical care by VA. Because GAO has not done any reviews which address these issues, the Committee has requested GAO to respond to two related areas of interest.

--First, you desire information which provides the historical perspective on Circular A-76.

--Second, you have asked that we cite examples of the types of reviews we have made concerning the implementation of the Circular, and the results of these reviews.

HISTORICAL PERSPECTIVE

ON CIRCULAR A-76

Government competition with private enterprise has long been a controversial issue. For over 40 years, congressional

committees have made many studies of the extent to which the Federal Government has competed with private enterprise in commercial or industrial activities.

In 1932, a special House committee made the first extensive study which found several commercial or industrial activities, created expressly for World War I needs, still in existence. Although the committee recommended terminating many of these activities, the Government expanded many of them and established new ones.

After World War II, congressional committees again directed their attention to commercial or industrial activities being performed by the Government as carryovers from the war years. Although military operations were their initial concern, studies of commercial activities of some civilian agencies were soon underway. The general finding of these studies was that the Government was involved in many unnecessary and nonessential competitive activities and that efforts should be made to discontinue any activity that the private sector could provide with reasonable convenience and at fair and reasonable prices.

In September 1952, the Department of Defense (DOD) issued the first in a long series of directives detailing policy and

instructions for commercial or industrial facilities operated by the military departments. The directive stated a policy against retaining and operating such facilities where required needs could be effectively and economically met by existing facilities of any other military department or by private commercial facilities. It also required the military departments to survey and justify continuation of existing facilities and restricted the establishment of new facilities.

In establishing the Commission on Organization of the Executive Branch of the Government in 1953, 1/ the Congress stated that it was its policy to eliminate nonessential services, functions, and activities which were competitive with private enterprise. In 1955, this Commission issued a series of reports which contained many recommendations designed to eliminate or substantially decrease those Government activities which were competing with private enterprise, and it urged the use of private contract services. One of these reports 2/

1/Public Law 83-108, 67 Stat. 142.

2/Subcommittee Report on Business Enterprises of the Department of Defense, June 1955.

points out several reasons why the Government should not do anything that the people are able to do for themselves. The reasons given were:

"It has been demonstrated over the years that the private enterprise system has been the best way to organize and develop the economic resources of our Nation. This system has resulted in the maximum production of goods and services with the minimum effort, * * *.

"* * * To the extent that Government engages in business enterprises, the base for taxation is reduced and larger taxes must be levied on individuals and industry. * * *

"* * * In private industry the initiative of individuals has been developed to a greater extent than in governmental activities. In private industry, it is possible to provide more adequate incentives in many instances and thus encourage new ideas and improvements, still maintaining competitive costs."

"* * * political control of what are essentially economic activities does not produce the effective results in Government business enterprises that are produced by the competitive and profit motives of private industry."

President Eisenhower's budget message of January 21, 1954, was apparently the first public statement of executive branch policy on Government competition with private enterprise. It stated:

"This budget marks the beginning of a movement to shift * * * to private enterprise Federal activities which can be more appropriately and more efficiently carried on in that way."

In January 1955 after months of study, the Bureau of the Budget (the predecessor of OMB) initiated a program to curtail some of the Federal Government's commercial or industrial activities. The policy of the executive branch subsequently evolved through four directives--three bulletins and one circular. 1/

1/Bulletin No. 55-4, Jan. 15, 1955.

Bulletin No. 57-7, Feb. 5, 1957.

Bulletin No. 60-2, Sept. 21, 1959.

Circular No. A-76, Mar. 3, 1966:

Transmittal Memorandum No. 1, Aug. 30, 1967.

Transmittal Memorandum No. 2, Oct. 18, 1976.

Transmittal Memorandum No. 3, June 13, 1977.

Transmittal Memorandum No. 4, Mar. 29, 1979.

Transmittal Memorandum No. 5, Sept. 26, 1980.

Although the basic policy of relying on the private sector to supply the Government's needs has remained the same, the guidelines and implementing procedures have been modified.

During the period in which the bulletins were in effect, several of the principal changes included the following:

- The policy emphasis was originally directed toward eliminating or preventing Government commercial activities. It was later recognized that, under certain circumstances, there might be compelling reasons which made it advisable or necessary for a Government agency to provide products or services for its own use.
- Under the initial phases of the program, procurement from commercial sources was strongly advocated without a comparison of relative costs unless the agency head concluded that the product or service could not be purchased on a competitive basis and at a reasonable price. This was later modified to recognize that, in some instances, commercial sources should be subject to competitive disciplines, including the possibility of Government production for its own use.

OMB, in 1966, departed from its original practice of issuing bulletins and issued OMB Circular A-76. Primarily, OMB wanted to restate the policy in a circular because a bulletin was generally considered to be a less permanent directive.

Circular A-76 and the three transmittal memoranda issued through 1977 reaffirmed the policy in the previous bulletins of general reliance on the private enterprise system. It identified, however, five circumstances of national interest under which agencies were authorized to provide needed products or services with their own resources. Further, it did not generally require agencies to make cost comparisons to support contracting-out decisions.

In March of 1979, OMB issued Transmittal Memorandum No. 4 and the cost comparison handbook (Supplement No. 1), and in September of 1980, issued Transmittal Memorandum No. 5. The effect of these revisions is to establish a three-part statement of basic philosophy: (1) Government reliance on the private sector is a valid principle, (2) certain functions are inherently governmental in nature and must be performed in-house, and (3) the taxpayer is entitled to economy in Government and cost comparisons are appropriate as criteria. Other major changes made in 1979 include a definition of governmental functions, a

listing of Government commercial or industrial activities that normally should be contracted, and a narrowing of the criteria for exceptions to the policy. Further, it generally requires that agencies make cost comparisons to support contracting-out decisions and that the savings through contracting should represent at least 10 percent of the estimated Government personnel costs.

EXAMPLES OF TYPES OF REVIEWS AND RESULTS

Our reports over the years have generally demonstrated a need for more effective implementation of the A-76 policy by the executive branch. They do not, as you might expect, support a broad conclusion that one method of performance (Government or private sector) is always preferred over the other. They do demonstrate that circumstances vary and each situation requires individual analysis.

DOD has devoted considerable time and effort to implementing the A-76 policy, and, consequently, most of our reports concern that agency. These reports involve a wide assortment of functions, ranging from individual types of services (aircraft fueling; airfield marking; custodial; food; guard; keypunch; laundry and drycleaning; maintenance of aircraft, construction

equipment, family housing, and motor vehicles; ocean cargo handling; supply, etc.) to total installation support for a number of services.

Basically, our more recent reviews have involved evaluations of either the propriety of a specific contracting-out decision at a given location or a more comprehensive review of an agency-wide or Government-wide nature, possibly involving several types of commercial or industrial activity. Our work in the first category is almost exclusively the result of constituency requests from individual members of the Congress and generally involve a detailed evaluation of an agency-prepared cost comparison.

A few examples of this type of work are as follows:

--We reviewed the contracting out decision of laundry services at Wright-Patterson Air Force Base, Ohio. We agreed that contracting out was more economical than in-house performance and estimated a substantially higher savings than the Air Force primarily because it had understated the number of in-house employees needed. (PSAD-80-17, December 7, 1979.)

--We reviewed the contracting out of 19 installation support functions at Fort Gordon, Georgia. The functions included, among others, maintenance, supply and service, transportation, and housing. We again agreed that contracting was more economical but estimated a reduced savings generally because the Army had overstated the number of cooks needed in the dining facilities. (PLRD-81-9, April 1, 1981.)

--In another request, we reviewed the contracting out of custodial services, laundry and drycleaning, and refuse collection at the U.S. Military Academy, West Point, New York. We agreed with contracting for the latter two activities but not for the custodial services. After making certain adjustments to the comparison, we concluded that the estimated savings were then less than the minimum required by OMB to justify contracting out. While the Army did not agree with our overall conclusion, it did agree that it had erred in its contracting procedures and agreed to make a new cost comparison. (PSAD-81-4, December 4, 1980.)

Our more comprehensive reviews are typically reviews of broad issues surrounding the A-76 program or reviews of major functions of a commercial or industrial nature.

A few examples of this type of work are as follows:

--We reviewed 12 DOD conversions to contractor performance to find out how much contracting out was taking place because of personnel ceilings, wage differentials between Federal blue-collar and contractor employees, and other significant influences. This work was done in response to concerns expressed by the Senate and House Committees on Armed Services. The functions we reviewed covered such activities as laundry and drycleaning, motor vehicle maintenance, aircraft maintenance, and total installation support of an ammunition plant.

We found that (a) the most significant reason for contracting out was that contractor costs were lower than in-house costs, (b) contractors' costs were lower because they planned to use fewer employees and pay lower wages, (c) although civilian personnel ceilings did not appear to be the primary reason for contracting out, the military services did use the A-76 program to reduce their

work force, and (d) questionable cost comparison practices influenced some decisions to contract out. (PLRD-81-19, April 22, 1981.)

--At the request of the Subcommittee on Defense, House Committee on Appropriations, we reviewed a sample of 18 conversions by DOD of a variety of activities covered by Circular A-76. One of our primary objectives was to determine whether decisions to contract out might have been different if subsequent contractor price increases and performance shortfalls were known before the contract awards were made.

Most of the conversions did not result in performance shortfalls, but we did find unsatisfactory contractor performance was experienced on 5 of the 18 conversions. However, where contract price increases occurred, they generally seemed to be justified. In addition to the five unsatisfactory performance cases, we found that one conversion decision was based on an incomplete statement of work which was used as the basis for the cost comparison. While it is possible that if the information we found after the fact had been known before the contract awards were made, different decisions might have been

made on these six cases, however, history doesn't provide alternatives. Unsatisfactory contractor performance was generally attributed to one or more of the following factors: high personnel turnover rate; unreasonably low staffing level resulting from a buy-in; untimely, improper, and/or poor quality work; too few skilled technicians; and inadequate training. (PLRD-81-58, August 26, 1981.)

--We performed a review which shows that the General Services Administration (GSA) is spending several million dollars more per year than is necessary to clean office buildings. Because of high wages and low productivity, GSA spent, in four regions studied, over 50 percent more to clean offices with its own custodians than with contractors, and almost twice what GSA landlords paid to clean Federal leased space. GSA is slowly converting to contract cleaning, but at the present rate this will take about 15 years. During this time, GSA may spend about \$250 million more than necessary to provide cleaning services with its more costly, less productive custodians.

We recommended that GSA make the comparative cost studies required by Circular A-76 to determine whether cleaning

services should be provided by its in-house staff or by contract personnel, and implement the results. We also recommended that GSA take specific actions to foster greater productivity and reduce costs of contract cleaning. (AFMD-81-78, August 24, 1981.)

--We performed another review which disclosed that Federal agencies use contractors, including consulting service contractors, to do work that we believe Federal employees should do because the work involves basic management decisions. The Departments of Energy and Defense, for example, used contractors to substantially determine or influence national energy policies, and identify requirements for national defense. Although contractors may not be making final decisions, we are concerned about the extent to which contractors are influencing agencies' control of Federal programs and policies.

Ironically, while some Federal agencies were using contractors for work that should be done in-house, they were also using Government employees to provide commercial services that contractors could provide in many cases at a lower cost.

We recommended that the Congress and OMB improve oversight and management of the Federal contract work force. (FPCD-81-43, June 19, 1981.)

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In closing, we would like to say that although its implementing guidelines could be strengthened, GAO supports the general policy precepts set forth by Circular A-76.

In 1978, we recommended, as did the Commission on Government Procurement in 1972, that the Congress establish a national policy relating to reliance by the Federal Government on the private sector to provide needed goods and services. (PSAD-78-118, September 25, 1978.) Without a firm national policy, the future of the A-76 program will be a repetition of the past--confusion, controversy, and ineffective implementation. The policy must be stable and must appropriately balance many issues of national significance. It needs both legislative and executive branch endorsement and support.

Mr. Chairman and Members of the Committee, this completes our formal statement. I will be happy to respond to any questions you may have at this time.

RESPONSE OF THE GENERAL ACCOUNTING OFFICE TO WRITTEN QUESTIONS SUBMITTED BY HON.
ALAN CRANSTON, RANKING MINORITY MEMBER OF THE SENATE COMMITTEE ON VETERANS'
AFFAIRS

QUESTION NO. 1: In its statement for today's hearing, the VA notes that "in a procurement budget of a little over \$2 billion, approximately \$700 million is for services which are classified as commercial/industrial." How does this proportion (over one-third) of contracting for commercial/industrial activities compare with the efforts of other departments and agencies?

ANSWER: Statistical data on agency contract services, presumably of a commercial or industrial nature that could reasonably be performed in-house, similar to that presented by the Veterans Administration is not available at GAO. Also, such data is not available at OMB. Apparently it must be provided by each individual agency. To the extent possible, however, care must be taken to ensure that the data is comparable.

QUESTION NO. 2: In your statement, you note that GAO conducted a review which shows that GSA is spending several million dollars more than necessary to clean office buildings and that contractors could do the work at less cost. Did you find that GSA could have taken steps to reduce substantially the costs of its doing the cleaning itself so as to more closely approximate a contractor's cost, or is such a differential inevitable?

ANSWER: There are steps GSA can take to improve the productivity of its custodians but we are not sure whether it can make sufficient improvements to offset the wage differential.

In our review, we found that GSA's cleaning standards, which it uses in staffing, were seriously outdated. They were developed in the mid-1960's and have not been changed to reflect the latest technology in cleaning methods, supplies, and equipment. For example, our analysis indicates that it is possible with new equipment to vacuum up to three times more area per staff hour than is required by the GSA standards. We concluded that establishment of up-to-date staffing standards, coupled with good supervision and issuance of procedures utilizing the latest equipment and supplies, are necessary steps to improve the productivity of GSA's in-house custodial staff.

QUESTION NO. 3: On pages 9 and 10 of your statement, you note three evaluations that GAO has conducted of A-76 cost comparisons. In each case, you pointed out problems in the cost comparisons that the agency had done. Doesn't that indicate to you that the costing techniques being used under A-76 are flawed?

ANSWER: Yes. Costing techniques can be flawed either by the use of faulty criteria or by the improper or non-application of sound criteria. Our work shows that the executive branch has cost comparison problems in both of these areas. Knowing that comparisons are only estimates and that they can never be totally accurate, the question then is whether the flaws are serious enough to affect the outcome in any given case. We believe that cost comparisons should be made, when it is appropriate to do so.

If the executive branch continues to improve the costing techniques, after focusing its attention on why faulty criteria exists and sound criteria is used badly, cost comparisons will more accurately and reasonably serve the purpose intended.

QUESTION NO. 4: Mr. Gilroy, when the Air Force submits its estimate of the savings involved in its "HAMS" contracts and I submit it to GAO for analysis and comment, would you please see to it that the analysis and comment are done promptly?

ANSWER: Yes.

QUESTION NO. 5: I would appreciate it if you would review the testimony of Mr. Kenneth Blaylock, the National President of AFGE, and the other union representatives who will testify today and provide the Committee with your comments on the statements in their testimony regarding the implementation of Circular A-76, most particularly please respond specifically to each point made about the flaws in the design of Circular A-76 that could lead the VA to entering into contracts on an inappropriate basis.

ANSWER: Our comments on the major points in Mr. Blaylock's testimony are as follows:

OMB and its Circular A-76 are openly biased in favor of contracting out

Based on our review of the comments offered and our work to date on the new Circular, we have not concluded that it is "openly biased" or that it "amounts to little more than blind, unyielding prejudice against performance of Government work by Government employees." Compared to the prior guidance, it does favor contracting in several respects but it also favors in-house performance in several others. If there is any overall bias, it is not readily apparent.

A-76 allows contracting out of governmental functions

Although Circular A-76 could probably provide a more usable and comprehensive definition of governmental functions, we do not believe it accurate to say that it allows the contracting out of governmental functions. As a practical matter, the Circular can only provide general guidance to serve as a starting point for agency officials who then have the primary responsibility for implementing its provisions, after considering their agency's particular circumstances.

A-76 forces contracting out regardless of cost effectiveness

Much of the discussion of this point centers on the importance of the statement of work to the cost comparison process

and a VA prototype statement of work for hospital services which allegedly fails to provide for special diets. Because we have not done any A-76 reviews at VA, we cannot address that agency's practices. As a general matter, however, the Circular recognizes the preparation of the statement of work as a critical step. It states that it should (1) be comprehensive enough to ensure that performance in-house or by contract will satisfy the Government requirement, (2) serve as the basis for determining both the contract and Government cost to ensure comparability and equity in the cost analysis, (3) clearly state what is to be done, and (4) provide performance standards to ensure a comparable level of performance with either alternative.

A-76 inflates the
in-house cost estimate

Our reaction to the examples used to illustrate this point is mixed. We disagree with the statement that A-76 conspicuously fails to require the in-house estimate to be based on the most efficient organization and staffing. We think that A-76 is clear on this point. (See Item 9c(1) of the Circular and Item D2, Chapter II of the cost comparison handbook.) Also, the reference to GAO's findings in this area implies that no organizational studies are being made. In a recent review of 12 Department of Defense contracting-out decisions, we found that required reviews were made in 7 cases. (PLRD-81-19, April 22, 1981.)

Regarding the statement that in-house estimates are often based on more expensive Government procurement systems as compared to contractors who can obtain their supplies and materials anywhere (an example is provided of OMB imposing a 21 percent markup on wholesale items ordered through GSA), we believe that the merit of the issue in individual cases depends on the comparability of the items in question and their base prices to which the 21 percent markup is added. It should be noted, however, that when we provided comments to OMB in December 1978 on the proposed cost comparison handbook, we said that the 21 percent wholesale and 36 percent retail markups were too high. Because we felt that the percentages could be as low as 4 and 21 percent, respectively, we suggested that they be determined by a new GSA study using as a basis only those indirect costs which vary with the volume of sales. Apparently, a new study was either not performed or was performed but it did not support changes in the proposed markups.

In calculating the cost of in-house operations, A-76 requires that a retirement cost factor equal to 20.4 percent of payroll be included in computing personnel costs. AFGE maintains that the addition of this factor is arbitrary, that it includes unfunded liability costs, and that it is sheer guesswork since OMB has never established the validity of the figure.

The factor is neither arbitrary nor based on guesswork. It was actuarially developed in 1979 by the Office of Personnel Management which is responsible for administering the retirement system. The factor represents the Government's share of the "normal cost" of the civil service retirement system. In pension terminology, normal cost (commonly expressed as a percentage of payroll) is an actuarial estimate of the amount of funds which, if accumulated annually and invested over covered employees' careers, will be sufficient to meet their future benefit payments. In essence, the factor represents the Government's share of the annual accruing cost of employees' future retirement benefits. In view of the fact that it represents currently accruing retirement costs, the factor does not include any past accrued unfunded retirement liabilities.

AFGE also claims that use of the retirement factor forces in-house cost estimates to include the cost of retirement over a thirty-year period while, in contrast, a contractor's cost estimate is based solely on outlays during the period of the contract. As mentioned above, the factor, when applied to the total salary paid to an employee over a given period of time, represents the estimated cost of retirement benefits which accrued during the same period. In the absence of any specific information, we cannot comment on what bases contractors may use in developing their cost estimates.

AFGE also stated that A-76 does not require that a factor for the unfunded liability of the social security program be added to contractors' cost estimates. Whether or not such a factor should be added is debatable. If it is assumed that, in the future, it will be necessary for the Government to contribute funds from general revenues to pay social security benefits, then the addition of such a factor may be appropriate. However, social security benefits have always been financed by a specific tax. Generally, current receipts from the tax are used to pay current benefits. In the past, increases in benefit payments have been financed by raising the tax rate. If this practice is expected to continue, then it would not be appropriate to add a social security cost factor to contractors' cost estimates.

Finally, we should mention that, based on a March 17, 1980, report by the retirement system's independent Board of Actuaries, the Government's current share of the system's normal cost is 29.5 percent. You will note that this factor is 9.1 percentage points greater than the factor currently prescribed by A-76.

A-76 also favors contracting out in other ways

This point addresses several aspects of how the A-76 policy is to be implemented, including various specific provisions of the cost comparison handbook, which are viewed as favoring con-

tracting out. Also, several administrative and legislative changes are suggested to eliminate the perceived bias. The implementation procedures quoted accurately reflect OMB's guidance. GAO, however, has not specifically reviewed or taken a position on these established procedures. We may take a position on those concerning cost comparison methodology in a forthcoming review.

The statements by Arte I. Pierce, President, National Council of VA Locals, AFGE, and Virginia O'Dell, President, AFGE Local 2547, provide remarks on (1) specific instances of past VA contracting-out experience, and (2) the potential future impact of contracting out on the cost of medical care for veterans and the level of services provided. Because we have not done any A-76 reviews at VA, we cannot address its past experience with contracting out.

Concerning potential future impact, our only comments are that agencies must, of necessity, lose some measure of control over their affairs when they contract out. Unless specifically exempted from Federal personnel laws, agencies are not to obtain support services through contracts which permit or require detailed Government supervision over contractor employees. A proper contract is one in which the relationship established between the Government and contractor personnel is not that of employer-employee. Further, the services must be of a type which can be properly delegated to non-Government personnel. Thus, agencies must rely on contractors and their employees to furnish the needed services of an acceptable quality, on time, at the agreed price. We prefer not to speculate on the potential future impact of such reliance by VA.

QUESTION NO. 6: On page 12 and 13 of your statement, you discuss briefly a review GAO did of a sample of 18 conversions by DOD activities covered by Circular A-76.

- A. Am I correct in my understanding that, of the 18 conversions reviewed, 5 had unsatisfactory contractor performance and a sixth was based on an incomplete statement of work--so that one-third of this sample demonstrated serious problems?
- B. Do you believe that this sample was atypical for some reason?
- C. You mentioned a variety of reasons for unsatisfactory contractor performance in the cases you looked at, including: high personnel turnover rate; unreasonably low staffing level resulting from a buy-in; untimely, improper, and/or poor quality work; too few skilled technicians; and inadequate training. How do you

recommend that an agency considering entering into a contract pursuant to Circular A-76 protect itself from such problems?

ANSWER:

- A. Yes, but as we noted in our report, we limited our evaluation only to the original contractors' price increases and performance shortfalls to the time of our review. We did this to minimize the considerable speculation which would otherwise be involved in trying to determine, after the fact, whether different conversion decisions would have been made if knowledge of subsequent events was known prior to the contract awards. For example, would a decision have been different if it were known beforehand that an original contractor would default during the fifth month of performance but that a successor contractor would perform satisfactorily? One can only speculate whether a replacement contractor would have performed better.
- B. No. Although we could not realistically use scientific sampling techniques, we do not believe that this sample was atypical. As our report states, the 18 conversions in the sample accounted for about 39 percent of the civilian positions eliminated by contracting out during the period selected.
- C. We believe that protective actions can be taken but that they only reduce the risk of problems and do not eliminate them entirely. In general, agencies should take several important actions both before and after a contract is awarded to better ensure good contractor performance of an A-76-type activity. Before award, an agency should make sure that the statement of work used to solicit contractor bids or proposals (1) accurately describes what is to be done, and (2) includes performance standards for later determining how well the contractor has met the work requirements. Also, it should adequately evaluate the responsibility of the potential contractor. After award, an agency should effectively administer the contract to ensure that the contractor furnishes the item or service of an acceptable quality, on time, at the agreed price.

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Chairman SIMPSON. It is my understanding from the testimony that OMB furnished us at an early hour today that they feel confident that they have precluded any major disruptions of vital services in case of a strike or unexpected default by the contractor and that that confidence apparently is based upon the A-76 requirement of having a minimum of two responsible bidders and that each bid must include prepriced options for at least two of the out-years. Do you know of any instances where these A-76 safeguards were actually implemented in the contract selection process but were insufficient to protect the contracting agency in the event of either strike or a default?

Mr. GILROY. I can't recall any incidents that we have looked at, Mr. Chairman, where this came into play, that is either strike or default. We have generally been looking at A-76 on a case-by-case basis, usually at the request of Congress. And I can't recall where any of these factors would have come into play.

Chairman SIMPSON. Mr. Gilroy, the committee would certainly welcome the recommendations of GAO on the issue of how to insure that cost estimates for inhouse performance and contractor performance are really, truly competitive, that they really are based on exactly the same, very tightly drafted statement of work. Also to the extent that this goal can be accomplished through legislative restrictions similar in kind to restrictions imposed by law on DOD contracting-out, we would be very interested in hearing your recommendations for any legislative provisions. Perhaps you could share that, or you could comment briefly on it now, knowing of course that what we are concerned with here primarily is the safeguarding of a most extraordinary national health-care system and that the recommendations you make take into account the uniqueness of that particular situation.

Mr. GILROY. I will comment briefly, Mr. Chairman. We have found in certain reviews that the cost studies that were done inhouse were lacking, particularly back in the period before 1980. I believe in one review we did for the Armed Services Committee we found that in 5 out of 12 instances the cost studies that were available may not have been good cost studies because required reviews to provide the most current and efficient type operation which could be readily compared to what the private sector was bidding on were not made and it was probably to the Government's detriment in those cases.

We have recommended that the services—most of our work has been in DOD because DOD has been the leader in this area—study all operations, CITA type operations, and come up with efficient work statements so that they know what is the best and most effective way to conduct these operations inhouse.

Chairman SIMPSON. We have reviewed that report entitled, I think it was "Factors Influencing DOD Decisions To Convert Activities From In-House to Contractor Performance," and there were some interesting questions I think that are relevant to this issue before us now. I was especially interested in the figures of the DOD medical center that you reviewed, the Brook Army Medical Center in Fort Sam Houston. You had indicated that the contract yielded only a 5-percent total savings, that no study was performed as required by the law, and that the actual cost of administering the

contract was about 60 percent higher than had been predicted. Would you inform us as to why that contract was then entered into at all, and is there cause to believe that that might occur again? Should we pursue it in this area?

Mr. GILROY. I am not sure what details we have on that. Let me refer you to Mr. Nagel.

Mr. NAGEL. I think what we found there, Mr. Chairman, could possibly happen in the other cases at other installations. When activities are being studied for contracting out, it is very difficult to determine, for example, what the cost of contract administration will be. Under the guidelines of the handbook, the standard factor of 4 percent is provided. Actual costs may vary from that. But the installations have been held to 4 percent.

Chairman SIMPSON. I think that obviously it seems to me that the problems come from these incomplete statements of work, SOW, whatever it is referred to in the acronym. Unreasonably low-cost estimates by a bidding contractor of course can result in serious disruption. How would you recommend preventing such problems from arising within DM&S?

Mr. GILROY. I think the statement of work which you mentioned, the SOW, is probably the most important problem, and it has to be current and complete. You have to look at the best way to do it and not necessarily what has been done in the past. And if you do this you will have a much more competitive base when bids or proposals come in from the private sector.

Chairman SIMPSON. You have presented us with some provocative material. Thank you very much. I appreciate your presence here. Senator Cranston will have some written questions for you, as will other members of the committee. Thank you very much.

Mr. GILROY. Thank you, Mr. Chairman.

Chairman SIMPSON. Next we have Mrs. Joan Kershner, director of the Veterans' Administration Medical Center in Columbia, S.C., and Dr. Howard Green, chief of staff of Veterans' Administration Medical Center in Vermont, White River Junction, and president of the National Association of VA Chiefs of Staff.

It is nice to see you again. So if you wish to proceed, we will certainly appreciate your views.

TESTIMONY OF JOAN S. KERSHNER, DIRECTOR, VETERANS' ADMINISTRATION MEDICAL CENTER, COLUMBIA, S.C., AND DR. HOWARD GREEN, CHIEF OF STAFF, VETERANS' ADMINISTRATION MEDICAL CENTER, WHITE RIVER JUNCTION, VT., AND PRESIDENT, NATIONAL ASSOCIATION OF VA CHIEFS OF STAFF

Mrs. KERSHNER. Mr. Chairman, we have not prepared a statement, but we will be willing to respond to any questions that you might have.

Chairman SIMPSON. Do you, Howard, have anything you wish to comment on?

Mrs. KERSHNER. Mr. Chairman, just listening to the Air Force presentation we have a slightly different situation. Many of the Air Force hospitals are small 30- or 40-bed hospitals. Most of ours are much larger hospitals. I am at a hospital with 400 medical and surgical beds, 120 nursing home care beds, as well as 60 psychiatric

beds. Our problems are greater in preparing statements of work than the Air Force. For example, our patients are elderly. They have sometimes not only have primary and secondary diagnoses, but tertiary diagnoses as well, while the Air Force cares for a younger population of active military and many dependents. So from that standpoint we differ.

My greatest concern about A-76 contracting is lack of flexibility and incidentally, I am not opposed to A-76 at all as it is a good tool of management. But contracting out large services does pose a problem. In addition to what I just told you, that is the size of our facility, we have assigned to our facility a satellite clinic in Greenville which is about 107 miles from us; we have the administrative responsibility for the Florence National Cemetery. We are the clinic of jurisdiction for the State of South Carolina. We administer the fee prosthetics program for the State and we do the laundry for the Charleston hospital every day as well as our own. For all this work we have a budget of approximately \$40 million.

When we set aside the salary dollars from that at the beginning of the fiscal year, and when we set aside the fixed contract dollars and the fuel and utility dollars, we have somewhat less than \$10 million left to use as flexible dollars to assign to our services or departments to administer. This past fiscal year just ended workload assigned and funded was for approximately 6,700 patients treated and 79,500 outpatients. As a matter of fact we actually treated 9,200 patients and over 100,000 outpatients. Now how do we do this with the same amount of dollars?

We have a remarkably good team, and it takes every service to form this team, not just the doctor and the nurse. A whole support arena is necessary with latitude and flexibility.

During the year and on a continual basis, we shift from one service the moneys assigned to them, when needed, and reassign to another. For example, if pharmacy has an extra demand to fill prescriptions, we may call the chief dietitian and ask her to serve the same kind of a menu with less expensive items on it but with the same nutrients, withdrawing moneys to then assign to the pharmacy, or similar money shifts may go on throughout many services and do.

If that flexibility is no longer there, and I say no longer, because in contracting out services contract dollars must be set aside and obligated at the beginning of a contract. As more dollars are moved into an obligated status my flexibility diminishes drastically.

Chairman SIMPSON. Let me, in that area, let's just put this question out and then you can both address it a little bit more specifically. Would you both comment on the potential effect of A-76 within the facility, and you have very well, Mrs. Kershner, the managerial flexibility, employee morale, the so-called team concept of hospital administration and other aspects of that sensitive relationship between management and support personnel?

Dr. GREEN. Senator Simpson, one of my major concerns is precisely that issue. Let me give a little bit of background. I think we are all aware, and I think physicians are becoming increasingly aware of the changing priorities in the Nation and the need to retrench. I don't think that is lost on us, nor do I think we are irresponsible in addressing the issue.

The VA hospital system, since it is directly controlled by Federal Government by an executive agency, is probably the most responsive to such problems, and we have a hospital system now that perceives itself to be under stress. I want to make the point, that we traditionally have not been funded at the same level of funding as the private sector, at least in personnel funds. The ratios in the private sector to do the same job are 3 to 4 to one versus our 2 to 1 at an outside estimate.

Within a hospital the hospital care team operates indeed as a team, and this includes dietary and building management people. For example, on the wards specifically, building management people will operate outside of the scope of their job descriptions. They are human beings and they perceive some of the problems the nurses, the physicians, and the rest of the team are having. They will frequently help out in doing things that are not covered by the impersonal job descriptions under which they work.

My concern is that when you develop a statement of work there is nobody who is wise enough to develop a total statement of work for all of the functions that occur. A contractor's prime function besides meeting the terms of his contract is to make a profit. That is why he is in business. Refusal to help out in addition to the restricted statement of work shifts workloads on employees who are already under stress.

I pointed out in the House hearings that that group of employees are nurses. Nurses are having unique problems as a profession and with their role in the health-care team. To shift the workload to nurses may well be the straw that breaks the camel's back and creates problems in hospitals that we may or may not be able to solve easily. That is my major concern, Senator.

Chairman SIMPSON. Mrs. Kershner, you spoke about the terrible—well, not quite that phrase—the difficulty in getting a design together of statements of work and yet could you not concur that in these certain areas it would not be difficult to design the statement of work, when we are talking about plumbing, steamfitting, maintenance, carpentry maintenance, electrical maintenance, and masonry maintenance. Other agencies now in the Federal Government have provided statements of work, and would not those be very helpful to you if we come to say a limited type of A-76 use?

Mrs. KERSHNER. Yes, sir, I think that we can work on statements of work and perfect them. It just takes someone's time to do that, and it takes time away from what they are already assigned to do.

Chairman SIMPSON. Indeed. Certainly that question you bring up, Dr. Green, about the nursing situation, is very real. The committee is aware of that. And certainly if there were a strike, say of support personnel supplied by an independent contractor, it would probably fall most heavily upon the existing nursing staff. But might I ask of you if at times when there is no labor disruption,

would not the nursing staff perhaps benefit from the presence of contract support personnel?

Dr. GREEN. Senator, that is a very difficult question for me to answer because it has to do with the number of personnel. In generic answer to your question, yes. If those contract personnel were over and above current personnel members, total numbers, sir. But a direct substitution of personnel under contract for the function I don't see would be of any benefit. If they were additional personnel, I think the nursing service would write a personal letter of thanks to the U.S. Senate.

Chairman SIMPSON. Nobody has ever done that before. We wouldn't know how to handle it if it happened. I understand.

Mrs. KERSHNER. Senator, may I comment on that?

Chairman SIMPSON. Yes, please, Mrs. Kershner.

Mrs. KERSHNER. What our real problem oftentimes is, related to additional workload over the anticipated or assigned workload. That is where the contract poses a difficulty. For example, most contracts have a flexible clause which allows increases or decreases within 25 percent. Last year at our facility we had an additional workload demand of 33 percent. No extra money is available to fund that immediately. It is an impossibility to find dollars to support the contract. However, with our own personnel we just spread them thinner and ask them to do more with less. It isn't that it is delightful or desirable to do so, but it is a necessity.

Our concern is to serve the veterans in our State, those who actually need care. Every day we weed out people who no longer need care. We also drop the nonservice connected out of the system. Last year we serviced 51 percent service connected in our outpatient clinics at the hospital and 72.2 percent at Greenville outpatient clinic. So we have done as much as we can, and yet there is an extra demand through increased applications for care and hospitalization.

South Carolina is in the Sun Belt, and we have a variety of new services available, the economy is tight, many reasons, but the point is we have these veterans seeking care. I have no key to lock the front door.

Chairman SIMPSON. Just out of interest, since you cite that outpatient figure, what was the percentage of nonservice connected in the inpatient category?

Mrs. KERSHNER. The national average is 70.5 percent. Our percentage is 70 percent for nonservice connected.

Chairman SIMPSON. Well, that figure would be over 50 percent if it tracks the national norm which is significantly higher than that. But that is very interesting to us. Really, the essence of what you are saying, Mrs. Kershner, is managerial flexibility is severely hampered by this as you see it.

Mrs. KERSHNER. Yes, sir.

Chairman SIMPSON. Even though we are dealing with such specific items as say, yard care or grounds maintenance, or that kind of thing, would it come to that?

Mrs. KERSHNER. If you recall, I mentioned that we have an outpatient clinic in Greenville. When that was opened we wrote into the contract that the contractor would provide building management services. The first year was a constant problem in that the

physicians and the nurses complained of inadequate cleaning. The second year we wrote what is now called a statement of work. We increased the definition of what we expected the building management services to be furnished by the contractor, and it was rather high. It was so high that we just couldn't afford it. Therefore, we decided that despite the fact that we had limited FTEE's available, we would provide adequate service to them because of their defined needs. We did at a much lower cost.

So we try to look at need each time to see what is the best to contract or not. We have been doing this for quite some time. We do have contracts. We have approximately \$1 million in fixed contracts at our hospital.

Chairman SIMPSON. I commend you on your dedication to your efforts. It is a tough job, and it is going to be tougher as we get into the further budget crunch, especially with a budget of \$25 billion, \$15 of it in entitlements, \$7 billion in health care, and where do we cut from there. And then with an emerging 65-year-old and older veteran population which will be coming on stream with the next few years that could very well overwhelm the system unless we deal with it. So thank you so much. I appreciate your testimony.

Mrs. KERSHNER. Senator, I just want to say, if we don't maintain our flexibility, we can hang it up.

Chairman SIMPSON. Do you think that Strom Thurmond on this committee would allow that to happen? [Laughter.]

Thank you so much.

[The responses of Joan S. Kershner, Director, Wm. Jennings Bryan Dorn Veterans' Hospital and Dr. Howard H. Green, Chief of Staff, Veterans' Administration Medical and Regional Office Center, White River Junction, Vt., to written questions submitted by Hon. Alan Cranston, ranking minority member of the Senate Committee on Veterans' Affairs, follow:]

RESPONSE OF JOAN S. KERSHNER, DIRECTOR, WM. JENNINGS BRYAN DORN VETERANS' HOSPITAL, TO WRITTEN QUESTIONS SUBMITTED BY HON. ALAN CRANSTON, RANKING MINORITY MEMBER OF THE SENATE COMMITTEE ON VETERANS' AFFAIRS

Question 1. What has been the impact of the increased emphasis on Circular A-76 at your facilities in terms of employee morale and what effect has this had on patient care?

Answer. It has been two years now since we moved to the new Wm. Jennings Bryan Dorn Veterans' replacement hospital. This period of time has been one of unusual stimulation. We feel that our employees have responded to this move and to our affiliation with the University of South Carolina School of Medicine in a very positive way. They work together as a team and have sustained a high level of interest in the changing role of our hospital. Thus, we assess the background employee morale level at our facility as higher than average. We feel that these factors may account for the absence of a truly significant impact of A-76 on employee morale, at least to the extent that such an impact would affect patient care. To be sure, our employees are concerned about A-76; in fact, I recently met with Food Service Workers and Engineering employees to answer their questions on A-76. The large conference room site of the meeting, was packed with employees who were truly concerned about A-76. The bottom line is that when an employee feels his job is potentially in jeopardy, his morale is bound to suffer in consequence. We attempted to allay our employee concerns by answering their questions and we did not sense that their morale had been impaired to the extent of detrimentally affecting patient care. We have heard, however, that in some facilities morale has been more seriously affected. We tend to think that the lack of a more pronounced negative effect at this facility is due to the good team spirit of our employees and also to the fact that A-76 impacts here have not progressed to the point of posing an imminent threat to employees. In addition to my meeting with the workers, the Associate Director and Chief, Personnel Service have met with the Union representatives to answer their questions and concerns about A-76.

Question 2. (Mrs. Kershner) If, as the result of the A-76 studies, you were required to contract the various services at your center and the cost of those services were to consume a substantial part of your budget, would this affect your overall ability to manage your medical center and, if so, in what ways?

Answer. Without a doubt, if we were required to contract for entire services at our hospital, this would detrimentally affect the overall ability to manage this hospital. The key effect results from the restricted flexibility that I would have to distribute limited resources in such a way as to manage an ever-increasing workload of outpatient visits and patients treated. The trend over the past few years has been one of decremental budget flexibility from a hospital management standpoint. Whereas workload has increased steadily and costs have continued to spiral upward, the recurring funding has not commensurately increased. For FY-81 just ended this facility was funded for an assigned workload of 79,782 outpatient visits. Despite our attempt to provide care for only those patients absolutely eligible and in need of care, we exceeded 100,000 outpatient visits, excluding 10-10. Similarly, our assigned

workload for patients treated was 6,728 while actually 9,200 were treated. Thus, we experienced more than a third more again the workload assigned to us for the fiscal year just ended. There is no key to lock the door when an assigned workload has been reached. Flexibility is the only key I have to successfully manage and address the health care needs of the veteran patient in South Carolina. For example, as a Hospital Director, I frequently need to adjust dollars from one hospital service, such as Building Management, in order to enable another service, such as the Pharmacy, to purchase needed supplies. The main problem with contracting out a large service -- such as food service -- is that a certain fixed dollar amount is committed at the beginning of the fiscal year and cannot subsequently be pulled back or adjusted as needed to balance the needs of other services. If a contract is developed based on an assigned workload and then an excess actual workload occurs as happened in the year just ended, I would have to withdraw money from other hospital services to supplement the contract. Whereas at present I can request the Dietitian to substitute more economical foods with an equivalent nutritional value in order to spread the available funds more thinly. The Columbia, South Carolina hospital provides care for 400 medical and surgical patients, 60 psychiatric and 120 nursing home patients. We maintain a satellite clinic in Greenville and have recently initiated a Vet Center there as well. We provide administrative support to the Florence National Cemetery. We are the clinic-of-jurisdiction for South Carolina, and, we are responsible for all fee prosthetics in the State. We also do the Charleston VAMC laundry. So that of the approximately \$40 million dollar budget allotted to accomplish this, we must lock up salary dollars, fuel and utilities and all contracts off the top. Further, we are constrained to use certain dollars as designated by appropriate line items in the budget. These constraints leave about \$10 million actual flexible dollars to manage. A hospital food service contract could easily consume a fifth of the remaining flexible dollars and would have to be obligated at the beginning of the contract. The fewer flexible dollars, the less responsible I can be to emergencies, increased costs, unanticipated regulatory charges such as water, gas, etc. Hospitals are unique institutions. A great variety of activities support the primary objective of patient care. Certain personnel wear more than one hat. From a management standpoint, it is not easy to coordinate these diverse activities and to ensure that they interact cooperatively toward accomplishment of our mission. One can imagine a situation in which a dozen or more hospital services are contracted out to different vendors. The Hospital Administrator, in this case, would have little management flexibility in extra staffing assignment such as infection control, quality assurance, meeting accreditation standards and many other areas. ~~yet it is inconceivable that under such circumstances the services would function cooperatively.~~ I feel that Veterans' Hospitals differ from businesses, industries, and other enterprises, in a very fundamental way. Even other hospitals in the private sector are better able to manage contracted services, because the costs involved are transmitted directly to the patient or third party payor. The unique constraint imposed on the Veterans Administration Hospital is a fixed budget. No

matter how great the workload in any given year, the hospital must operate within a fixed limitation on funding. Our concern is that we will be unable to provide the high level of care to the patient that we have been providing when the preponderance of our flexibility to appropriately and legally manipulate resources is taken away.

Question 3. As health-care administrators, what are your personal concerns generally about Circular A-76?

Answer. The main concern we have is the one addressed above, namely, the inevitable restriction or constraint on our flexibility to manage resources. However, in addition to this concern there are several others which deserve to be mentioned. For example, in regard to food service, the question that I have had to ask myself as a Hospital Director is, "What is it that makes a food service chain competitive?" In my opinion, the principal reason is the difference in personnel costs. Federal agencies have more restrictions on hiring than the food service contractor does; but it is important to note that our hiring restrictions fulfill a service which is an expressed desire of Congress. Many people whom we hire would be considered underqualified by a contractor. We not only are obliged to hire and train these people, but we are also obliged to grade them according to the job grading standards determined by the Office of Personnel Management. Thus in our hospital, a cook must be graded at level WG-4 which in our area begins at \$5.40, whereas in the local community, an unskilled cook may be hired and put to work as a cook at the minimum wage. We perform a hidden service because we make people employable by teaching them a skill or trade, good work habits and often other remedial skills; the contractor does not have this obligation or a commitment to this type of job applicant. As you can understand, this effort is in concert with the National Economic Recovery Goal. Since CETA and some other retraining programs have been either abolished or drastically reduced, our efforts as described are among the few which provide the service to the given select population. Another related reason that we are not competitive with the private sector in food service costs is that we must buy our supplies from a mandatory source listing, i. e., Depot, GSA, small business, female and minority-owned business. We do not regard this concern as a major issue but one which needs to be mentioned. Often the price that we pay for a contract food item is considerably greater than the local retail cost of the same item. However, we emphasize again that in purchasing supplies from small business and minority-owned businesses, we are performing a service which is desired by the Congress. Food service is more closely related to direct clinical care than say, for example, keypunch. This causes additional concern, especially should the contract go to a small or relatively unproven vendor. During the past several years, there has been increased evidence to support nutritional evaluation and care of patients as part of the overall treatment plan. There has been a continually evolving clinical philosophy regarding nutritional care of the patient. Suppose in a hypothetical instance a physician orders some new, more expensive nutritional supplements for a particular patient. The Clinic Dietitian now has two masters -- the hospital and the contractor. Can we be sure

that the contractor will not say, "Sorry, we can't do this because it's not on the list." While this is not a major concern, it is an example of one of our concerns. A far greater concern is one in which the contractor fails to perform acceptably, either because the quality of food or service is poor, bankruptcy occurs, emergencies arise or a variety of factors create a problem or lack of service. If a contractor does not perform in the private sector, the administration can go to the Board of Directors and their lawyer and terminate the contract. In the years that I have worked for the Federal Government, it has been incumbent on Government to prove unequivocally that the contractor is at fault. I doubt that I could give even five instances where we have won a case in a timely manner. The decision invariably favors the contractor and may be drawn out for an indeterminate length of time. We shudder to think how difficult it would be to assemble a work force from scratch. At best, it could take 60 days to get an inhouse food service reasonably trained and reactivated using the present hiring policies as determined by the Office of Personnel Management and to effect the first purchasing and delivery mechanism for a smooth operation. Another problem is that of accountability. Food service workers will presumably be accountable to the contractor; however, the Hospital Director is ultimately accountable for all patient care. Another minor point, but one that consumes your time and ours is complaints. Most patients, either in private or public hospitals, are apprehensive on entering the hospital and are not objective judges of the quality of their medical treatment. However, most patients know whether the food is acceptable or whether the hospital is clean. We foresee the possibility that justified complaints from patients may neither be easily nor timely resolved. In conclusion, I would like to emphasize that we are not opposed to contracting out as a general principle, in fact, with the ever-increasing complexity of health care technology, no hospital could possibly employ all the technical personnel needed to keep sophisticated equipment operational. Our facility contracts for nearly \$1 million of services per year. We feel positively toward the role of private enterprise in the Veterans Administration health care delivery system, but nevertheless, we remain concerned about the feasibility of contracting services which are closely allied to direct patient care.

RESPONSE OF DR. HOWARD H. GREEN, CHIEF OF STAFF, VETERANS' ADMINISTRATION MEDICAL AND REGIONAL OFFICE CENTER, WHITE RIVER JUNCTION, VT., TO WRITTEN QUESTIONS SUBMITTED BY HON. ALAN CRANSTON, RANKING MINORITY MEMBER OF THE SENATE COMMITTEE ON VETERANS' AFFAIRS

Question 1. Impact of the increased emphasis on A-76 at your facility in terms of employee morale and effect on patient care.

Answer. There has been a definite decrement on employee morale. One could hardly expect less when a group of employees are threatened with potential loss of jobs. Certain employees in our dietary division have started to come in early and leave late in order to get in a little more work. This is in clear violation of the Fair Labor Standards Act which puts the onus on management to prevent these practices. In short, morale is at a low ebb and this is spilling over to unaffected services. I cannot clearly identify an effect on patient care that I could unequivocally support on hard scrutiny.

Question 2. What is your personal professional view on the impact on patient care of contracting out for non-direct care functions in a Medical Center, such as food services or housekeeping services?

Answer. The point that must be appreciated is that the VA hospital system is a system under extreme stress. It is understaffed in comparison to comparable community facilities. We are not able to put proper support help behind our professional physician and nursing staffs. The people assigned to dietary and cleaning management services frequently help our nurses do little things that are not within their job descriptions. This varies from running errands to answering an occasional telephone or to clean up a mess on short notice. These people become unofficial members of the team. This element of care has a major potential for getting lost in a contract. By default the load would be borne by the nurses. I need not recount for you the tenuous situation we have already in our ability to recruit and retain nurses. In short, I am opposed to mandatory contracting of patient support services based on cost alone. Any such contracts must be carefully examined by local management for all of the implications.

Question 3. As Health Care Administrator, what are your personal concerns generally about Circular A-76?

Answer. The principal major concern is the limitation on management flexibility which will be imposed by the widespread use of this tool. Mrs. Kerschner has stated the case well. I am also concerned that this kind of micro-management based on cost considerations alone by OMB is contrary to the best interests of the Veterans Health Care System.

Chairman SIMPSON. The next witnesses, the veterans groups. Mr. Riffin will not be present and will submit his testimony in writing for the record. We have Phil Mayo, special assistant, national legislative service of the VFW; Charles E. Joeckel, Jr., assistant national legislative director of the Disabled American Veterans; Gabriel Brinsky, national service and legislative director of AMVETS, and Michael F. Delaney, national president of the Paralyzed Veterans of America.

It is good to see you all. Welcome to the committee.

Mr. JACKSON. Senator Simpson, I am accompanying Mike Delaney. I am George Jackson.

Chairman SIMPSON. Fine. Nice to have you here.

TESTIMONY OF A PANEL OF REPRESENTATIVES OF VETERANS' ORGANIZATIONS CONSISTING OF PHILIP R. MAYO, SPECIAL ASSISTANT, NATIONAL LEGISLATIVE SERVICE, VETERANS OF FOREIGN WARS; CHARLES E. JOECKEL, JR., DEPUTY NATIONAL LEGISLATIVE DIRECTOR, DISABLED AMERICAN VETERANS; GABRIEL P. BRINSKY, NATIONAL SERVICE AND LEGISLATIVE DIRECTOR, AMVETS; AND MICHAEL F. DELANEY, NATIONAL PRESIDENT, PARALYZED VETERANS OF AMERICA, ACCOMPANIED BY GEORGE JACKSON

Chairman SIMPSON. So if you will proceed. We appreciate having your testimony.

Mr. MAYO. Thank you, Mr. Chairman. I am Phil Mayo from the Veterans of Foreign Wars. We would like to thank you for inviting our views on OMB circular A-76 as it applies to the Department of Medicine and Surgery of the VA.

First of all, I would like to thank the Committee for advancing into law, Public Law 97-66, a provision of which relates to the restriction of the use of VA funds for the purpose of A-76 cost comparisons. We note that OMB has asked that this provision of the law be repealed, and we find this abhorrent to take health-care funds and divert them from care of veterans into accomplishing these comparisons.

We are not convinced at all that the implementation of A-76 would serve the best interests of our Nation's veterans in obtaining health care of the highest caliber. We believe the best interests of the veteran will be served by not implementing A-76.

We also note, Mr. Chairman, that approximately 64 percent of the VA's employees are veterans, and A-76 would jeopardize the employment of many of those employees.

I would be happy to respond to questions you may have.

Chairman SIMPSON. I notice that all of your testimony supports really a flat exemption. You are uniform on that, an exemption from DM&S from the terms of A-76. However, recognizing that DM&S has had some successful experiences contracting out, and recognizing that there are some commercial and industrial functions within DM&S that I think can have no impact on direct patient care, such as media services, outdoor grounds maintenance, interior design, window washing, is a flat exemption really appropriate?

Mr. BRINSKY. Good morning, Mr. Chairman.

Chairman SIMPSON. Good morning, Gabe, how are you?

Mr. BRINSKY. Fine, thank you. The flat exemption I think which we have in mind, Senator, is not that resort wouldn't be made to some of these services, but that there is no need for providing for such services, such as required in A-76. I think we all agree that there are any number of services that can be performed. But we at AMVETS feel that this should be a managerial decision. The determination as to whether resort should be made to the private sector should lay with management.

Chairman SIMPSON. I am sorry, Gabe, would you repeat that? I want to hear your response.

Mr. BRINSKY. I think basically our position at AMVETS, Senator, is that undoubtedly there are many areas where contract services

are desirable and are cost effective. We believe, however, that management should have the flexibility of resorting to these services as it sees fit. And we don't believe that management should have its hands tied by being required to follow a specific directive.

Chairman SIMPSON. Mr. Joeckel.

Mr. JOECKEL. Also, Senator Simpson, doesn't the VA currently have the authority to do that? I believe they have the authority to contract where they deem necessary. We are concerned over the mandate from OMB to contract things that normally the VA would not be looking into. And we are specifically concerned about direct health care—however that might be defined. We believe this question is best left to Dr. Custis and certainly not to OMB.

I would like to address some of the things that I noticed this morning that—

Chairman SIMPSON. If you could, yes, within the limits of trying to keep specifically your objections as veterans groups in this area. I am trying to develop the reason for your firm decision that there should be a flat exemption without any kind of flexibility, rather than reviewing and rebutting other more general arguments. But please proceed, I don't want to cut you off, but we don't have that much time to go into the full—

Mr. JOECKEL. First, we don't think there has been enough experience. Those witnesses other than the VA, who appeared today were unable to relate to you what their experiences have been. They indicated that they would like to submit that information for the record.

As far as our organization is concerned, we would not want to contract direct health care, patient care. I think you have to look at some of the things that make up total health care—food service, laundry, service and some other things that back up and support what doctors and nurses do. The record is not clear there as to what the experience has been.

The OMB indicates that they have more sophisticated ways of writing statements of work and the picture looks very rosy, but still no experience. That is why our organization will continue as mandated by the convention to oppose A-76. I will be happy also to answer any other questions. I think our statement is very clear.

Chairman SIMPSON. It is indeed.

Mr. Delaney.

Mr. DELANEY. Yes, Mr. Chairman. PVA would concur with the statements of the other veterans organizations on that point.

We also feel that the Administrator now has the authority to contract for outside services. In fact, I think the chief medical director indicated that he is doing a great deal of that, and I believe the figures were much higher than the Air Force had indicated in their testimony. So the ability to contract is there, and we feel it is a managerial decision and should be done on a case-by-case basis as opposed to a direct blanket policy directive.

Chairman SIMPSON. Of course one of the things about the VA and its activities in contracting out is that I think that the VA already contracts out nearly \$700 million for services of various sorts. So it is not a strange proposal for them, and the statements of work have obviously been presented when they are expending

that amount. And that includes many of the services we are now talking about.

In fiscal year 1981 approximately \$9 million was spent for contracts for automated data processing related services, \$72 million for maintenance and repair services, including upkeep of roads, walks and grounds, \$15 million for veterans counseling service, and \$23 million for the repair of equipment.

So I just wanted to see if there was any flexibility there in your position, because there has been some work experience, and there have been some obvious areas which at least to me, do not affect direct health care or are not inherently governmental or have no overriding factors requiring in-house performance.

Mr. JOECKEL. We have no disagreement with that. Our organization has become alarmed about certain things that were listed in the original A-76 circular which seemed to be involved with the direct health care delivery system.

Now we have been assured time and again by OMB that there is no grand scheme. However, I think DAV would rather associate itself with what Senator Cranston had to say this morning. In spite of all the assurances that we have gotten, time and time again the same ideas come forward. Last year when we discussed Gramm-Latta with OMB, they assured us there was no scheme to demise the health-care system, and later they asked us to support Gramm-Latta. In turn, we asked for their assurances in writing. We weren't provided their assurances in writing, and accordingly we didn't support Gramm-Latta. Until we do get it in writing I don't think we can be too happy about contracting out health-care services.

Chairman SIMPSON. Well, I know, but if we continue to live on what did happen in the past, we are not going to be very productive or helpful to each other at all. I don't think those are helpful references. Let's remember that at the time all that occurred we didn't have a VA Administrator, we didn't have a Deputy, we didn't have an IG, and you had a Senator taking over the chairmanship of the committee who had been around the joint just about 2½ years. Sure there are some aspects to examine if you want to go back and continue to trot it out. I don't think it is productive. I wouldn't want to limit you in your desire to do so, but I am afraid I will be tuning it out most of the time because I don't think it has much to do with the issue.

The issue was that when we had a confirmation hearing on Robert Nimmo he was very specific on what he was going to do, and he has not retreated one bit on that. So let's just stay in the here and now instead of washing old laundry from time to time. We will watch Robert Nimmo. I am going to observe him carefully and see how he does. I have read his testimony in all areas very carefully, and if everything that comes up is viewed with suspicion, then certainly his effectiveness will not be enhanced. And there is much to be done.

Mr. BRINSKY. I just want to make one observation, Senator. Since the VA has the authority to contract out these services, we personally have a lot of confidence in Dr. Custis and his abilities as a manager as well as a physician. I think the fact that the Department of Medicine and Surgery has been increasing the amounts of

money that it has been spending on a contract-out basis, I think this points toward a trend. And actually I think what is being accomplished is what the circular wants, but without the restraints of the circular or the direction or discipline, if you would, of the circular.

Mr. JOECKEL. Well, I just wanted to state quite clearly that we would not look on most of these things with suspicion if we had opportunity for input and communication. We do look forward to working with Administrator Nimmo in these areas. You know we have been working with you.

Chairman SIMPSON. Indeed.

Mr. JOECKEL. Our experiences over several years with OMB have not been that delightful. If we can develop that kind of rapport, that would be good, too.

Chairman SIMPSON. I understand. I remain accessible to you or to any other group, as does the committee staff. I do appreciate your testimony. It is helpful in the full mix. Thank you.

Mr. DELANEY. Mr. Chairman, if I could.

Chairman SIMPSON. Yes, sir.

Mr. DELANEY. I would like to ask that our full testimony be read into the record. It has been given to the committee staff.

And I would like to make one other point. I would like to take exception to the testimony given earlier by the representatives of the U.S. Air Force who perhaps overstated the success that they feel that they have had with the contracting experience in the Air Force.

Overall we think experience will show that it has not been all sugar and spice, and perhaps they were looking through rose-colored glasses. For example, in doing our research we came across some figures that indicated that the Air Force in rushing toward greater contracting experienced some adverse results when its statement of work greatly underestimated the contractor's assignments.

It is fortunate that the events at the Air Force Academy concerned only the cleaning of the floors in the fieldhouse and similar buildings and not hospitals. But the fact of the matter is that as a result of the underestimation that occurred in the contractor's assignments that as a result the 3-year contract price had to be increased by about \$708,000. That is just one instance where the SOW was underestimated. I think that perhaps they overstated, or understated their position and perhaps should have indicated more of the problems that they have had with the contracting as opposed to the successes that they have had.

Chairman SIMPSON. Very important, and it is something that the committee is aware of.

Mr. MAYO. Mr. Chairman, if I may.

Chairman SIMPSON. Yes, Phil.

Mr. MAYO. I would like to observe that we are in times of greater financial stress insofar as VA has been in, to my knowledge, than ever before. I think the more we contract things out, or services out in the VA, the less able the VA is to meet those stresses.

I am not aware myself of any contractor who would accept a lesser amount of money for performing as great or greater services

as can be done with the flexibility that we currently have in the VA.

Mr. DELANEY. If I could make one final point, Mr. Chairman, and I will finish. I think another thing that we have to ask ourselves here is, you look at the Japanese today in industry. What is the reason that they have been so successful? Time in and time out we found out that the loyalty factor amongst their employees seems to be the difference between their high productivity levels and our lack of productivity. I think loyalty is one aspect that you can't really equate with dollars and cents. And in the system today we have loyal employees. I think we have to give strong consideration to that aspect when we talk about contracting further services out. We are going to lose that, and that loyalty is very important to the operation of the Veterans' Administration today.

Thank you very much, Mr. Chairman.

Chairman SIMPSON. Thank you all. We appreciate your testimony.

Without objection, the complete written statements of all of the veterans' organizations will be entered into the hearing record at this point.

[The prepared statements of Philip R. Mayo, special assistant, national legislative service, Veterans of Foreign Wars of the United States; Gabriel P. Brinsky, national service and legislative director, AMVETS; Charles E. Joeckel, Jr., deputy national legislative director, Disabled American Veterans; and Michael F. Delaney, national president, Paralyzed Veterans of America, follow:]

VETERANS OF FOREIGN WARS OF THE UNITED STATES



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PREPARED STATEMENT OF

PHILIP R. MAYO, SPECIAL ASSISTANT
NATIONAL LEGISLATIVE SERVICE
VETERANS OF FOREIGN WARS OF THE UNITED STATES

BEFORE THE

COMMITTEE ON VETERANS' AFFAIRS
UNITED STATES SENATE

WITH RESPECT TO

IMPLEMENTATION OF OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-76
(CONTRACTING WITH THE PRIVATE SECTOR FOR SERVICES PERFORMED IN-HOUSE)
BY THE VETERANS ADMINISTRATION

WASHINGTON, D. C.

NOVEMBER 5, 1981

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

Thank you for the opportunity to present to you the views of the Veterans of Foreign Wars of the United States with respect to the contracting by the Veterans Administration for services currently performed by the VA as provided for in the Office of Management and Budget Circular A-76.

Mr. Chairman, we commend this Committee on their foresight in the passage of what is now Public Law 97-66, the "Veterans' Disability Compensation, Housing and Memorial Benefits Amendments of 1981." That measure contains a much needed compensation and dependency and indemnity compensation payments increase, along with other provisions which we believe effect compensable veterans and their dependents in a positive fashion both now and in future years. Those provisions relate to the increase of the insurance coverage for certain veterans up to \$35,000; improvements in automobile adaptive equipment benefits; improvements in specially adapted housing assistance benefits; and, important in the Committee's deliberations today, provisions

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which restrict the VA's (and the OMB's) freedom to conduct cost comparison studies that may lead to the contracting out of important functions within the Department of Medicine and Surgery (as required under OMB Circular A-76, and which would cause an estimated reduction in personnel of perhaps 30,000) and which require the VA to submit major reorganization plans for congressional review nine months prior to their effective date. This latter provision relates primarily to the recent attempt to reduce the functions of the 58 VA Regional Offices into three (thereby causing the dismissal of approximately 1,600 personnel within the Department of Veterans Benefits).

It is important to note, Mr. Chairman, that the VA has indicated that 3,880 studies (at a cost of \$29.1 million) would be required to comply with the Circular's cost comparison review requirements. Additionally, the conducting of a priority review of three auxiliary functions (plant maintenance, food service, and custodial service) would require 1,480 studies at an estimated cost of \$10 million. We find it abhorrent to reduce health care and related services by approximately \$40 million in order to accomplish these comparisons.

As you are aware, Mr. Chairman, the issue of contracting with the private sector for goods and services currently being provided by the federal government--in this case the Veterans Administration--has generated considerable controversy. It should be noted at the outset that we believe the President and the Executive Branch of the government are bound to faithfully execute the laws enacted by this body--the Congress of the United States. In that connection, where a conflict occurs in the implementation of an executive policy such as found in OMB Circular A-76 and what we perceive to be the clear and unmistakable intent of Congress, we believe the law and the expressed intent of Congress should prevail until such time as Congress indicates otherwise.

Our understanding of the transmittal memorandum accompanying Circular A-76 underscores the concept that while the general policy of the government is to contract with the private sector, based on the premise that in a democratic system

government should not compete with its citizens or private enterprise, it fully recognizes that certain functions are inherently governmental in nature and must be performed by government personnel. The memorandum further limits the scope of its intent insofar as the definition of exempted functions are concerned when it exempts those functions "which must be performed in-house due to a special relationship in executing governmental responsibilities," including those functions that necessitate the discretionary application of government authority as in the management of programs requiring value judgments (such as national defense) and the selection of program priorities.

We also note, Mr. Chairman, that our interpretation of current law would preclude OMB from causing the VA to contract its basic health-care function. Public Law 79-293 created within the VA the Department of Medicine and Surgery (DM&S) under a Chief Medical Director, with its primary mission being to provide a complete medical and hospital system for the care and treatment of veterans. We reiterate that this is a national policy established by an act of Congress.

In keeping with the policy that the Veterans Administration shall provide such care, Congress has carefully guarded the granting of any authority allowing for contracting of services--even to veterans. Chapter 17 of title 38 details Congress' will by specifically enumerating the role of DM&S as a provider of hospital, nursing home, domiciliary and medical care, restricting that care to eligible veterans within the limits of the VA to provide that care. The VA is permitted to contract with private entities to provide care, but this authority is restricted to certain beneficiaries--particularly when the care involves a non-service connected condition. "Fee basis" or contract care, under Public Law 94-581, was authorized where VA or other federal facilities were not capable of furnishing economical care because of geographical inaccessibility or of furnishing the type of care or services required. Other areas of contracting under title 38 have also been specifically restricted as well--for example: the areas of research and insurance, scarce medical specialist

services, and specialized medical resources. In addition, numerous other sections of title 38 express the will of Congress regarding hiring, qualifications, and pay, among other criteria, of many IM&S employees. In short, Mr. Chairman, it is our view that Congress has specified the extent it deems appropriate for the contracting of IM&S's functions and we view as presumptuous the disregard of congressional intent exhibited by the Office of Management and Budget in its attempts to implement the provisions of Circular A-76 within the medical care system of the VA.

As you are also aware, Mr. Chairman, the VFW periodically surveys the hospitals operated by the Veterans Administration for the purpose of assuring a continuing high level of care for our veterans. These surveys necessarily include every facet of the hospital's operations, and they are conducted by our Field Representatives who are all experienced in assessing the ability of VA hospitals to function as they should. These individuals have repeatedly reported their conviction that the imposition of OMB Circular A-76 in areas directly impacting patient care would, literally, be catastrophic to the VA hospital care system. Their concerns are as follows:

1. There would be a loss of control by management and service chiefs where they would not be able to deal directly with employees, but would be required to deal with the contractor.
2. Many good, reliable and motivated VA employees would be lost. There is no assurance that current VA employees would be engaged by a private contractor.
3. It is believed that the team concept used in building management, engineering, and other services of a hospital would no longer be as effective.
4. The employee/patient relationship would most likely cease to exist.
5. The real possibility of a lack of concern and compassion for patients on the part of contracted employees.
6. A contracted employee would not be available for or under any obligation to perform collateral duties.
7. Further difficulty would occur in the coordination of

various activities between services.

8. An increase in equipment abuse and possible theft is anticipated.

Similar concerns, Mr. Chairman, were expressed before the House Veterans'

Affairs Committee on October 20, 1981:

"My name is Gary Mullennix, President of Huntington Laboratories, Inc. of Huntington, Indiana. Our company manufactures and sells housekeeping products to the institutional market. We also sell our products to some 2,500 hospitals across the United States and are well known within the trade.

"I want to thank the Committee for the opportunity to testify on the merits of the proposal for using outside cleaning contractors under A-76. I hope my efforts will be of value.

"As I understand the proposal under A-76, I must say that no businessman would ever knowingly expose himself to the risks inherent in such a scheme. Turning over a large, costly and critical function to an outside contractor whose primary goal is to produce a profit sets up a constant conflict of interest.

"The additional peril caused by surrendering all VA supervisory and housekeeping personnel into the direct employment of the contractor is frightening. The result can only be a total loss of control over the delivery of quality health care. This scheme further ensures a dramatic rise in housekeeping costs because it removes any real options the VA might have to return to an in-house operation or to employ another contracting firm.

"The reason is quite simple. The threat of the then current contractor's removal of all 'his' housekeeping employees means the VA would have to accept virtually any terms offered. Each contract renewal would be tantamount to a strike. No housekeeping duties would be performed and the delivery of Health Care would cease...

"The hospital's only recourse would be to magically produce--instantly--a fully trained housekeeping and supervisory staff. It would be impossible.

"There are no options worth exploring. This proposal is an idea which should be stopped here and now...

"There are many other serious problems that need to be addressed in considering the use of an outside contractor... For now, let's pick a few of the more obvious problems.

1. Teamwork - An outside contractor whose goal is to make a profit cannot build a loyal team. Since the employees report to the manager of an outside company who can fire them, their loyalty to the hospital evaporates. When a conflict of interest arises, they will side with the contractor.

Also, rapid termination of housekeeping employees to achieve the desired staffing level will sow the seeds of discord that will grow for years.

Finally, the contractor's manager will not cooperate with the other managerial team members when a conflict arises...

2. Management Development - As businessmen, we know that our future success is dependent upon the quality of the managerial team we assemble and train. Our responsibility to the corporation is that, should we vanish tomorrow, or any one of our departmental heads vanish, the organization moves along without a hitch.

It is poor management practice to abrogate that responsibility to an outsider over whom we have little control.

3. Loss of Supervision - In most contracts, the hospital agrees to not hire away the management staff of the contractor. This becomes a strong argument against getting out of the contract, since to do so means the hospital has no trained supervisors on hand. No hospital should put itself in this position of weakness.
4. Loss of Accountability - Employee personnel records, housekeeping procedures, reports on inspections, condition of equipment, inventory and requirements of supplies are all the property of the contractor. We caution any hospital contemplating leaving the contractor to make every effort to regain this material before notifying the contractor of the hospital's intention. Again, this occurs because the contractor is an outside agent, not an employee of the hospital. The loyalty is outward...

"The solution to providing high quality housekeeping is readily available. It takes an effort and commitment by administration to get the job done. The tragedy is to mistakenly pass the responsibility to an outsider who can only do what the hospital could do for itself. And, the hospital can do it at a much lower cost while delivering the highest quality health care."

Mr. Chairman, before that same Committee, Mr. Albert L. Condino, an hospital Administrator, with over twenty years experience as such, provided his insight regarding contracting:

"In summation, from my experience, I conclude that:

1. A profit-making contract service cannot perform at the same level at a lower cost regardless of what their multitude of brochures and salesmen may say. They can begin with a 'sweetheart contract' just to get their foot in the door, but that is where it ends.
2. The management control over a contract service department is not the same as the direct control over your own hospital department which is so essential to administering an effective hospital operation.
3. The morale of the contract service employees is lower because their wages and benefits are significantly less than the hospital employees' wages and benefits because of the need for the contract service company to show a profit.
4. The hospital administrator who goes to contract services is copping out of his/her responsibility to the institution as its chief executive officer to manage an efficient and effective hospital."

On July 9, 1981, Mr. Chairman, the Honorable Dan Daniels (Va.), with others, made a compelling statement on the floor of the House regarding contracting out of services in Armed Forces hospitals. We invite your attention to his remarks in the CONGRESSIONAL RECORD of that day:

"Mr. Chairman, as reported by the Committee on Armed Services, H.R. 3519 contained section 304 which prohibits the use of any operations and maintenance appropriations authorized therein for the contracting out of entire military medical facilities. In addition, the committee deleted \$15 million in specific authorizations in the Army, Navy and Air Force requests associated with contract conversions.

"The reason for these actions is that the committee found itself confronted by a proposal that has virtually no redeeming qualities. It is not justified on the basis of shortage of military medical personnel. It is unlikely to result in any cost savings and/or increased efficiencies. It is operationally unsound. And it cannot be defended on the basis that it falls within the normal operations of Office of Management and Budget (OMB) Circular A-76. As will become apparent in the course of this debate, contracting out entire medical facilities was never envisioned by A-76 and should have been totally exempted under the eligibility criteria set forth in that document.

"The impetus for this proposal originated in 1979 in response to severe problems the services were experiencing in the recruiting and retention of military medical personnel. Whatever justification exist-

ed at that time has disappeared due to corrective actions by the Department of Defense and Congress to address personnel-related deficiencies. Although shortages remain in certain critical specialties, their remedy is not to be found in the contracting out of entire military hospitals.

"While contracting out of military medical facilities has been under study since 1973, there is no hard evidence that it would result in any significant cost savings. In fact, earlier efforts failed because contractor bids greatly exceeded in-house estimates. More recent efforts to develop comprehensive statements of scope of work upon which to base cost comparisons have only confirmed the futility of attempting to address unique military requirements within a civilian contracting-out framework.

"The committee's paramount concern, however, is that the contracting out of military medical facilities would have a serious adverse readiness impact by denying their use to train military health professionals and help them maintain skills required on the battlefield. Equally important the military physicians staffing these hospitals provide a ready pool for rapid deployment for direct combat support. The degradation of military medical readiness has been consistently and forcefully stressed by the three service Surgeons General in testimony before Congress opposing this proposal.

"Finally, the committee's prohibition does not threaten the integrity of OMB Circular A-76 for the simple reason that its contracting-out provision should have never applied to military medical facilities. By A-76's own eligibility criteria, the unique military character of this activity and its inherent readiness implications should have exempted it from consideration. In fact, the Office of the Secretary of Defense (OSD) had to override service recommendations to exempt these functions from contracting-out for national defense considerations. It is another case where OSD has seen fit to subordinate commonsense and military requirements to social or political ends.

"In sum, the committee finds that contracting out entire medical facilities is not warranted in terms of cost or efficiency. In terms of readiness impact and the chance of increased wartime mobility, it makes no sense at all.

"In view of the foregoing and OSD's own unwillingness to abide by the spirit and letter of OMB Circular A-76, a specific prohibition against the contracting out of entire medical facilities was included as section 304 of H.R. 3519."

One VA Medical Center Director recently observed, when his Senator inquired as to the impact of Circular A-76 on his facility, that:

"We are, as you can appreciate, very troubled about the possible disruption in and lowering of standards in the care we

render veteran patients at this center. The majority of patients are suffering from emotional illnesses requiring patience, acceptance, tact, diplomacy, and above all, empathy from all of our employees and volunteers. We are not at all confident that these special qualities and sensitivity to the needs of patients will be found in people who have no prior special interest in the patient and the treatment or rehabilitation programs of the Department of Medicine and Surgery."

Mr. Chairman, it is also well-known that the VA is one of the major employers of veterans. By reducing the number of VA employees, the number of veterans employed in federal service would be automatically reduced. In contemplating the prospect of increased contracting for goods and services by the federal government, the voting delegates to our most recent National Convention adopted Resolution No. 622 entitled "Oppose Contracting of VA Services." This resolution resolves that we undertake to cause the cessation or reduction of any contracting out of government services now being performed by in-civil service personnel that would adversely effect the recruitment and retention of veterans. A copy of that resolution is attached hereto.

Mr. Chairman, we would also point out the experience of the VA in contracting its laundry services. According to the best information available to us, the contracting of that service has not yielded the desired result. We are cognizant of cases where the cost of doing the laundry of certain facilities has escalated tremendously over what the cost to the VA would be had an in-house laundry been maintained. We believe bids on such contracting may have been made at levels whereby the business would be secured by the private contractor, and once the terms of the original contract had been met, the VA was then subjected to questionable pricing demands when it had no ability to accomplish this service on its own. We are concerned that contracting of other services vital to patient care will yield similar results, thereby causing the ruination of our VA medical care system.

In conclusion, Mr. Chairman, we do not believe the requirements of OMB Circular A-76 should be applied to the medical care system (DM&S) of the VA. We believe that Congress intended the federal government to provide for the health care

of those who have defended our nation--and this does not include contracting for such care. This fact is demonstrated throughout title 38, United States Code. To impose A-76 on DM&S would remove the necessary management flexibility needed in that system in order for it to operate smoothly and efficiently--for our veterans and not necessarily for budgetary convenience. We believe that in title 38, Congress has established the parameters it deems appropriate insofar as contracting for care; and we believe the imposition of further contracting on the part of the Executive Branch to be an unwarranted and unjustified avoidance of congressional authority and intent.

This concludes my testimony and I would be happy to respond to questions you may have at this time.

Resolution No. 622

OPPOSE CONTRACTING OF VA SERVICES

WHEREAS, an area of increasing concern is the contracting out of service within the Veterans Administration as proposed by the Office of Management and Budget Circular A-76; and

WHEREAS, the implementation of such a drastic change in the method of providing service at Veterans Administration Health Care facilities will tend to affect adversely the quality of care of the veteran increasing the potential of employee strikes; and

WHEREAS, the use of commercial contractors will tend to create problems of untold magnitude and will disrupt the cohesiveness essential to the effective direct and indirect patient care operational capability of Veterans Administration health care delivery; and

WHEREAS, contracting out of patient care services in Veterans Administration Health Care facilities is in no way comparable to the contracting out of business-commercial type services in other agencies not related to health care both in the federal government or the private sector; and

WHEREAS, the continuing contracting out of services will seriously jeopardize veterans employment rights and represents an attack on veterans preference laws diminishing the number of full-time jobs otherwise available to war veterans; now, therefore

BE IT RESOLVED, by the 82nd National Convention of the Veterans of Foreign Wars of the United States, that we and the Congress strongly resist and urge the Veterans Administration to oppose any further attempt by the Office of Management and Budget to implement the provisions of OMB Circular A-76.

Adopted by the 82nd National Convention of the Veterans of Foreign Wars of the United States held in Philadelphia, Pennsylvania, August 14-20, 1981.

PREPARED STATEMENT OF GABRIEL P. BRINSKY, NATIONAL SERVICE AND
LEGISLATIVE DIRECTOR, AMVETS

Good Morning. It is our understanding that this Committee will hear testimony on OMB Circular A-76, the cost of its implementation versus potential cost savings within the Veterans Administration Department of Medicine and Surgery, and its specific ramifications for the provision of medical care by the Veterans Administration.

In view of the enactment of Public Law 97-66 which was signed by the President on October 17, we will not comment upon the cost of implementation of the Circular versus the potential cost saving features since the Law precludes the Veterans Administration from conducting any further studies on the feasibility of contracting out. As this Committee is aware, the Congress has indicated that no further step should be taken to implement Circular A-76 cost comparison studies in the VA health care facilities unless the Congress has expressly made such funds available for that specific purpose. As a note in passing it may be observed parenthetically that the VA estimates that it would cost 29 million dollars for the approximately 4 thousand studies required under Circular A-76.

At the onset I might indicate that AMVETS has no argument with the over-all concept of OMB Circular A-76 insofar as it relates to competitiveness and the selection of the most cost effective services.

What is wrong, as we view it, is that its provisions are too broad in application and fail to take into consideration good managerial precepts which are applied on a continuing basis. Perhaps more importantly, it fails to take into consideration that certain services, such as health care, cannot be evaluated or measured in terms of dollar values.

We take some comfort from the opinion of the General Counsel of the Veterans Administration issued last year which held that OMB Circular A-76 does not apply to hands on care in the Veterans Administration health care facilities, which by the way OMB originally disputed as a valid interpretation but which it now accepts.

We also find the provision of Public Law 97-66 most helpful which prohibits cost comparison studies in VA health care facilities unless the Congress makes funds available specifically for that purpose. It is our understanding that the Office of Management and Budget has indicated its support of the VA General Counsel Opinion that under current statutes, OMB cannot direct the VA to contract out its basic health care functions.

Since recent legislation has limited the scope of our concerns, in deference to the time restraints imposed by this Committee, we request that our detail statement be admitted to the record and we will confine ourselves to a few brief observations.

AMVETS believes in the competitive system, as we stated earlier, and we embrace the concept of utilizing services which prove to be most cost effective. But at the same time we are also convinced that there are certain services which cannot be measured or equated in terms of money or dollars. There are certain products in the form of services which do not lend themselves to a profit or loss evaluation and any attempt to do so in terms of

services provided by the Veterans health care program would be anachronistic.

Concededly, there are some functional services of the Veterans Administration health care program which could lend themselves to cost effectiveness studies, nonetheless we feel there is a caveat. And that is that cost itself even in functional services should not be the sole criteria in determining whether or not resort should be made to contracting out. For there are other important considerations such as the effect that such a functional service may have upon a hands on care aspect of the health care program.

It seems to us that what might well be a management decision is being denied those who are responsible for the ongoing effective operations of the health care program. In our opinion, A-76 seems to ignore managerial responsibility for introducing cost effective savings in all phases of its operations. What functional services could be let to competitive bidding should be a management decision.

For example, under Department of Medicine and Surgery of the Veterans Administration and whose operations this Committee is primarily concerned, of 622 million dollars expended in Fiscal Year 1980 for maintenance, repair and operation of VA health care facilities, almost half of that amount was expended through contract services. And the trend seems to be towards an increased reliance upon the private sector for various functions such as ambulance service, garbage and refuse collection, plant maintenance, insect control, etc. This tendency has occurred because of improved management techniques and realizations. In our view, management should continue to exercise its expertise in the realm of realities as exist under given circumstances rather than by following stereotyped dictates of a written instruction.

In conclusion, AMVETS is opposed to the application of the provisions of OMB Circular A-76 to the Department of Medicine and Surgery of the Veterans Administration in any of its operations. We believe that a more effective system can be accomplished through the use of managerial prerogatives as determined within the purview of existing circumstances.

The Veterans Administration including the Department of Medicine and Surgery, moved to implement the requirements of OMB Circular A-76. The underlying approach of the Veterans Administration was to take action to reduce the growth of federal spending while ensuring that the government does not compete for business with its citizens. And, underlying its actions, the Department of Medicine and Surgery viewed the opinion of the General Counsel of the Veterans Administration, dated March 21, 1980, as controlling. That opinion emphasized that the Department of Medicine and Surgery's direct medical care responsibilities mandated by Title 38 of the United States Code is not subject to A-76 review.

The Veterans Administration was proceeding to implement the Circular by meeting two specific requirements outlined by the OMB. Specifically, to complete cost reviews for hospital food preparation, hospital custodial, and hospital plant maintenance not later than the end of fiscal year 1982; and to complete cost reviews for susceptible functions by the end of Fiscal Year 1983. The Department of Medicine and Surgery was proceeding on the basis that the function of food preparation and delivery may be appropriate for contracting but that the clinical and administrative aspects of the Dietetic Service are to be retained in-house. This was before the enactment of Public Law 97-66.

AMVETS is of the view that OMB A-76 should not be applicable to the Department of Medicine and Surgery of the Veterans Administration simply for the reason that in health care the elements of quality and service have no cost factor. For example, there is no way ever of measuring an ineffectual custodial service upon the overall affects of an affective health care program. The operation of a hospital requires the coordinated efforts of cohesive units. The loss of control over one or more of these units can have repercussions upon the operation of other units. Concededly, while there may be contractual functions which can be performed outside of the

Department, we suggest that these are limited even within the scope of custodial or maintenance requirements.

Historically, a revision of OMB Circular A-76 became effective on May 1, 1979. In a Subcommittee Hearing on the Committee on Post Office and Civil Service, the Office of Management and Budget testified in effect that government functions should be performed by federal employees while products and services that can only be provided in the private sector should be obtained by contract. In all other cases, cost-effectiveness should be the deciding factor.

The Subcommittee in the First Session of the 96th Congress, was considering HR-4717 which would amend Title 5, United States Code, to provide for adjustments to federal personnel ceilings based upon the extent that federal functions are contracted out, to provide the performance in administering personnel ceilings and contracting out requirements are taken into account in evaluating the performance of Federal Executives and Managers, and for other purposes. The Bill was intended to discourage the practice of contracting out for personnel services by requiring an offset of federal personnel by reason of the reduction created by the contract personnel. The motivators for this legislation came from the federal employees union which have advocated that there should be legislation to limit contracting out of personnel services.

It was the intent of HR-4717 to eliminate wasteful contracting out.

Report 96-729, Part I, notes that during the Eisenhower Administration there was an emphasis by the Executive Branch on Contracting for Goods and Services needed by the federal government. The thrust of the Executive Branch was to look to the private sector first for needed goods and services. This practice brought into being the policy established by

OMB Circular A-76 issued in 1966 and amended in 1967. Proponents of outside contracting argued that the government should not compete with the private sector. Opponents reasoned that the government's increase in contracting for services of an inherently government nature lost control of its own programs by doing so.

In its deliberations on HR-4717, the Subcommittee was concerned with the problems of personnel ceilings and the performance of functions which are inherently governmental.

The Subcommittee in its report stated: "...Office of Management and Budget Circular A-76, revised (March 29, 1979)(hereinafter Circular A-76). Section 5.f. of that circular defines a "governmental function" as "a function which must be performed in-house due to a special relationship in executing Governmental responsibilities." It is then noted that "Another consideration is that products and services which only the private sector may feasibly provide should be obtained by contract.... This recognizes that in some instances it is not feasible for the government to provide products and services, and in those cases the products and services must be obtained by contract. The final consideration is cost and it is obvious that the intent of the proposed legislation and the concerns of the Office of Management and Budget is in the direction of cost effectiveness as determined by governmental functions and feasibility."

Therefore, it is apparent, that the entire issue of contracting out was raised with a view of avoiding personnel ceiling limitations but contracting out regardless of its cost effectiveness. Under the practices which did occur, the number of employees allocated to an agency under a statutory or administrative personnel ceiling limitation was not reduced

when at the same time the agency contracted out functions which were assigned to its personnel. The positions were retained and on occasions they were used for other purposes. Therefore, the costs of the agency were not necessarily reduced. It was the intent of HR-4717 that the personnel ceiling of the agency would be reduced when the functions were contracted out and savings from the reduction in personnel would result.

At the same time it is recognized that frequently agencies are prohibited from performing work in-house because of personnel limitation even though it would cost less to do them with federal personnel than by contracting out. Under OMB Circular A-76 it is required that the agencies review all commercial and industrial activities performed by federal employees to determine whether the function could be performed at less cost by a private concern.

It is the view of AMVETS, considering the report 96-729, Part I, of the House of Representatives, and HR-4717, which was introduced in the First Session of the 96th Congress, that the intent and purposes of OMB Circular A-76 should not be considered as being applicable to the functions and operations of the Department of Medicine and Surgery of the Veterans Administration. As we regard the legislative history, the intent and purpose of contracting out was not to encourage it, but to limit it. It was to eliminate it as a vehicle for disregarding personnel ceilings. In our opinion, the Department of Medicine and Surgery should not be considered as a "commercial or industrial activity" and as such being subject to the requirements of Circular A-76.

In addition for the reasons stated, we are of the view that the focus on cost effectiveness completely disregards the elements of service and quality which have no cost value factors. The reduction in cost factor in no way equates for a reduction in quality which is a non-equatable factor.

Obviously, A-76 will require an analysis and comparison which will result in hundreds of hours of accumulating and processing the data required under its provisions.

To summarize, we would make the following points: (1) The legislative history and intent of the provisions of Circular A-76 was never intended to apply to operations such as the Department of Medicine and Surgery of the Veterans Administration. (2) Should the Department of Medicine and Surgery of the Veterans Administration be considered as within the scope of OMB Circular A-76, then the following adverse affects can be expected to follow:

- a. The Management's flexibility and ability to respond to unusual circumstances will be adversely affected.
- b. A contractor's default can only be dealt by cancellation of his contract. As expressed in Report 96-729, we share the Committee's concern over the numerous instances of "buy-in" pricing by contractors who have failed to deliver.
- c. When a default occurs who will perform the day-to-day duties in the interim? The facilities provided by the agency prior to the contracting out will have been dismantled and no longer operative.
- d. Dismantlement of equipment or an operation with waiver of historical knowledge and the expertise gained over years and the maintenance of an operation or equipment is lost. A start-up operation if necessary, would entail once again initial operating cost.
- e. A short-run savings may result by reason of an initial bid by a contracting service. It is not unusual, however,

to have initial bids unreasonably low but to be followed by unrealistic increased in future. The problem posed is that once a facility divests itself of its ability to perform a particular task, to resume its past role can result in uncontrollable cost.

It is our understanding that with the enactment of Public Law 97-66, the Veterans Administration is precluded from further implementation of OMB Circular A-76 in the Department of Medicine and Surgery. Nonetheless we are concerned that the \$100,000 provision for contracting out under certain conditions may have its impact upon the health care program. As stated earlier, we are of the view that contracting out should be made at a managerial level based upon the prevailing circumstances rather than according to a disciplined, structured formula.

In conclusion, AMVETS is of the opinion that A-76 should not be applicable to the Department of Medicine and Surgery of the Veterans Administration: If it is considered as being within the purview of the Circular, it ignores the elements of quality and service which have no cost factor.

PREPARED STATEMENT OF CHARLES E. JOECKEL, JR., DEPUTY NATIONAL
LEGISLATIVE DIRECTOR, DISABLED AMERICAN VETERANS

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

On behalf of the nearly 700,000 members of the Disabled American Veterans, I am pleased to appear here today, Mr. Chairman, to discuss the impact of the implementation of the Office of Management and Budget Circular A-76.

Let me begin by expressing to you and the members of this Committee our sincere gratitude for your willingness to conduct this hearing, in order to insure that the funds required to conduct cost comparison studies relating to the OMB Circular A-76 are not taken from certain VA health care accounts.

As you know, Mr. Chairman, recognizing that the private enterprise system is the primary source of our national economic strength, it has been the policy of the government for quite some time to rely upon competitive private enterprise to supply the government with products and services. Such a policy was first recognized as early as 1955 and in March 1966 Circular A-76 was issued for the first time.

So the concept of government reliance on the private sector for goods and services is nothing new. What is new, Mr. Chairman, is the fact that the current revision of OMB Circular A-76 proposes to contract to private enterprise nearly every facet of maintenance and service presently performed by federal employees.

It is interesting to note that the current revision of Circular A-76 points out in its background material that the federal government should not place itself in the position of competing with private enterprise. In general, we concur in this assessment.

However, we contend that in terms of veterans' benefits and services--particularly in the area of health care--our programs have never been a part of the private enterprise market. Since World War II, at least, veterans' health care, for example, has been provided exclusively by the government through a federally owned and operated health care system.

It can be said then that veterans' health care has not been, over the years, a market which has been stolen away from the private sector. Further, in our view, there is no competing interest in the private sector which seeks to provide medical care to all current eligible veterans at a cost equal to or lower than that presently provided through VA's system of hospitals and outpatient clinics.

In this connection, Mr. Chairman, I would like to point out that last summer the Veterans Administration completed a study which showed that VA medical care is 18.3 to 22.5% less expensive than similar care provided by comparable private health care facilities. According to this study, it would have cost American taxpayers nearly one half billion dollars more to send eligible veterans to private health care facilities. Further, care at a VA hospital for an average medical episode last year cost \$2,480. The same care extended in a community hospital would have cost \$2,981--over \$500 more. The average episode of surgical treatment in the VA last year cost \$3,255 while the same care at a non-VA facility would have cost \$4,061--over \$800 more.

OMB Circular A-76 seems to assume that outside contractors would provide the same quality of work as VA employees. However, part of the reason, in our view, that VA medical care costs less, rests with the fact that its services are provided in-house by the thousands of dedicated federal employees who have at heart a genuine interest in the welfare of veterans. What price can be placed upon the dedication demonstrated daily by VA personnel?

At the center of the controversy--regarding VA health care, at least--is an issue solely related to rising federal expenditures and health care costs. We have already demonstrated that medical care provided by the VA is cost effective. But, there are other considerations--I alluded to one a moment ago, dedication.

Permit me to discuss some of the others, Mr. Chairman.

Strikes

What would happen if a VA hospital contracted out for some essential service--food preparation, for example--and the contractor's employees decided to strike? Such a job action could bring a VA medical facility to its knees, possibly forcing the facility to close until the contractor settled the employee dispute.

Poor Quality Work

What would happen if a company under VA contract did poor quality work? As you know, Mr. Chairman, firing a company that holds a contract with the federal government can be a long, drawn out, expensive process. VA hospital administrators could easily be forced to put up with inferior work until the contract runs out.

Increased Cost

What happens when a contractor submits a short-term, undercutting bid against which VA employees cannot compete? The contractor could take his losses during the first Fiscal Year and, when the VA has lost its ability to handle the work in-house, the contractor could demand an increase in the price of the contracted services.

Management Control

Difficulties with contractors is not the only problem VA officials would be faced with. Implementation of OMB Circular A-76 would fragment the management of the VA health care system. Each time another service is contracted out, hospital administrators would lose that much more control over the operation of the facility.

Management of individual hospitals and of the system as a whole would become incredibly complex. A new layer of VA management would be needed to negotiate contracts, coordinate the activities of contractors and make sure employees of the contractors are getting the job done.

Carried to its extreme, OMB Circular A-76 could force the VA to contract whole hospitals for the care and treatment of veterans. Then, what kind of control would the agency have over the quality of care provided to veterans?

Mr. Chairman, the VA has had experience with the contracting out of its services, some of the problems I have just referred to have already occurred in the VA.

For example, here is what happened at the VA Medical Center at Cheyenne, Wyoming. The Veterans Administration contracted

with a service to clean its laundry. The linen wasn't cleaned well enough, it wasn't delivered on time, and less linen was coming back to the medical facility than was being sent out. Finally, the Medical Center terminated its contract with the private firm and now it sends its linen to the VA Medical Center in Denver for laundering.

The VA Medical Center in Reno, Nevada was sending its laundry to a sole-source contractor until the contractor increased the price of services by some 100%. In addition, the Reno medical facility had to pay out \$80,000 to replace linen and other laundry items that had turned up missing or were not returned from the laundry on time. This VA facility is now having its laundry done in Sacramento, California.

As you know, Mr. Chairman, the VA has authority contained in Section 213 of Title 38, U. S. Code, to contract with private enterprise for services performed in VA facilities. To a great degree, the VA already utilizes this authority when, quite naturally, contracting for services economically works in favor of the VA without interrupting services provided to veterans.

Currently, VA contracts approximately \$700 million of its commercial/industrial activities. These figures were recently released by VA officials' testimony on similar hearings held by the House Committee on Veterans Affairs on October 20, 1981.

In our opinion, it would be interesting to know why the VA does not contract for even more services and what the experience with contracting out has been in past years. We suspect that a requirement for additional contract services, beyond that which VA currently authorizes, would not be beneficial to the VA both in terms of efficiency and cost effectiveness.

The Administration insists that its program to curtail federal spending, as well as, its intention with respect to OMB Circular A-76, will not interfere with direct patient care. However, Mr. Chairman, if the VA is required to contract its health care services to the degree currently proposed in A-76, it will, in our view, have a direct adverse impact on the health care provided to veterans.

You simply cannot operate a hospital with direct health care personnel alone. Every service plays a significant role in carrying out its mission of providing for the adequate care and treatment of veteran patients.

Recognizing this, the delegates to our most recent National Convention held last July adopted Resolution #528 opposing the contracting out of services in VA health care facilities. The resolution states in part that the Disabled American Veterans ...seeks the enactment of legislation which would grant to the

VA's Department of Medicine and Surgery an exemption to the provisions of the Office of Management and Budget's Circular A-76. Accordingly, we are grateful to you, Mr. Chairman, and the members of this Committee for your willingness to include provisions in recently enacted legislation (P.L. 97-66) that prohibits the VA from using funds from certain VA medical care accounts for the purpose of carrying out cost-comparison studies required by OMB Circular A-76.

This concludes my statement, Mr. Chairman, and I wish to again thank you and the members of the Committee for giving us this opportunity to express our views on this important subject.



PREPARED STATEMENT OF
MICHAEL F. DELANEY, NATIONAL PRESIDENT
PARALYZED VETERANS OF AMERICA
BEFORE THE
SENATE COMMITTEE ON VETERANS' AFFAIRS
CONCERNING
OMB CIRCULAR A-76
NOVEMBER 5, 1981

Mr. Chairman and Members of the Committee, it is an honor for me to speak today on behalf of the members of Paralyzed Veterans of America. PVA consists of approximately 12,000 members, all of whom are veterans who have experienced spinal cord injury or dysfunction. We are very familiar with the health care services offered by the Veterans Administration through its Department of Medicine and Surgery.

PVA is grateful to this Committee and its leadership for conducting this investigation of the Office of Management and Budget's Circular A-76 and the effects it would have on veterans health and medical care. This Circular would have the VA health-care system contract with private providers for many of the services now provided in-house by VA employees.

In the Federal Register of July 29, 1981, there appeared a listing of functions for which the VA would seek contractors, should the provisions of Circular A-76 be implemented. These topics include food preparation and delivery services; medical records processing, storage, and retrieval; prescription services, pharmaceutical pre-packaging services; appointment scheduling, and hospital sanitation services.

The Office of Management and Budget (OMB), in proposing application of Circular A-76 to the VA health-care system, seeks to save money. PVA, as a veterans service organization, seeks to have the VA provide veterans with the maximum number of quality health-care services possible. Because there is limited funding available in any Congressional appropriation, PVA seeks to have the VA save operating costs whenever reasonably possible. We seek both efficiency and effectiveness, goals similar to OMB's but also significantly different from its concentration purely on reducing the cost of operations.

In PVA's view two aspects of Circular A-76 must be examined; its likely effects on the VA's ability to care for veterans health and medical needs and its likely effect on the cost of these services to the American people. There are other areas which need examination, also, and we will attempt to discuss them briefly after looking at the quality of VA services and their cost.

Americans have always understood their obligations to the Nation's veterans and have always sought to fulfill that duty. We are a Nation of citizen soldiers, and unlike a country which hires mercenaries for protection, we rely on ourselves to serve the Nation in its times of need. The Constitution of the United States has established it as a basic principle that one of the federal government's functions is

to provide for the national defense: veterans medical and health care services are part of the cost of national defense in our society. Veterans health care, as provided through the VA's Department of Medicine and Surgery (DM&S), is an appropriate area of responsibility for the federal government, and this is a permanent duty which exists even if an era is philosophically dedicated to reducing the role of the federal government.

Several circumstances surrounding implementation of A-76 cause PVA great concern. First, OMB has required that studies be conducted at each VA facility for each VA function which is the subject of contracting. We agree that potential major changes in the VA's operations should be studied thoroughly; however, to meet OMB's demands would cost the Department of Medicine and Surgery approximately \$30 million, and OMB did not provide these funds. Rather, it commanded the VA to fund the required 3,880 studies out of monies to be provided by Congress for veterans medical and health care. In short, OMB did not consider the needs of veterans when it made its demands on the VA. As the Honorable Virginia Smith (R-Nebraska) recently asked rhetorically of this \$30 million, "How many renal dialysis procedures, chemotherapy administrations, and fitting of prosthetic devices could be paid for with such funds?"

PVA recognizes that usage of general medical funds for conducting these studies is largely a moot point now, since passage of Public Law 97-66, the "Veterans' Disability Compensation, Housing, and Memorial Benefits Amendments of 1981." PVA would like to sincerely thank the Members of this Committee and of both Chambers of Congress for including language which prohibits use of DM&S appropriations for A-76 studies unless specifically authorized by Congress.

PVA continues to worry about the source of funding for these cost comparison studies: the Senate has not yet taken action on the Conference Report for the HUD-Independent Agencies Appropriations Bill for 1982, and OMB presumably spoke as the President's economic and fiscal advisor when it originally advocated denying many veterans needed services in order to finance these studies. OMB either did not understand that, because of budget restraints, the VA is already hardpressed to care for eligible veterans, or OMB did not care if veterans were denied health-care services. Only specific legislation can protect veterans' health care services.

As noted, PVA's goal is for eligible veterans to receive through the VA the maximum number of quality health-care services, even if OMB does not share our goal. We must look closely at the types of services which will be available, should the VA rely increasingly on contractors for services now provided by VA employees.

The VA has relied on contract services whenever it has found that these services are superior to those which the VA could provide, or whenever it has found that contractors can provide services of satisfactory quality for less cost. For example, the VA has concluded that it is less expensive to contract with local ambulance operators than to attempt to provide these services in-house. And, the VA has had to contract for use of highly sophisticated medical-care equipment whenever VA facilities do not contain them. In short, the VA has always attempted to consider the needs of veterans, the cost of services, and the availability of care. Through years of continuous operations and practical experience, the VA has learned, generally, how to weather funding restrictions and at the same time fulfill its obligations to eligible veterans.

A sudden shift to greater contracting does not reflect the tried and proven approach to contracting which the VA has developed, and even the 3,880 studies mandated by OMB are not to study function--they are to study only cost. Perhaps we should learn from the Department of Defense, which moved rather suddenly toward the replacement of many in-house functions by contract services. In 1979 Congress restricted DOD's ability to have private contractors provide services and last year these limitations became permanent. (Public Law 96-107 and Public Law 96-342) Section 502 of Public Law 96-342 (the "Department of Defense Authorization Act of 1981") states: "No commercial or industrial type function of the Department of Defense that on October 1, 1980, is being performed by Department of Defense personnel may be converted to performance by a private contractor." This Section is qualified, however, and the Secretary of Defense may use contract providers, but only if contractors can maintain suitable standards and only after the Secretary has reported to Congress that he intends to seek contracts for specified services. (These are basically the same guidelines which control the Administrator of Veterans Affairs without implementation of OMB Circular A-76.) In short, Congress has found that reliance on private contractors to perform public functions has warranted tighter controls and closer examination, if the military is to be able to respond quickly to emergencies and if personnel are to understand their duties and work as a team.

The Veterans Administration moved toward increased reliance on contract providers, and the quality of results has been mixed. As noted, the VA relies on contractors for services which are used irregularly and thereby do not warrant a standing VA labor force to provide them. Or, the VA contracts for needed specialized equipment and services when Congress has determined that this

reliance is preferable to appropriating greater funding so that the VA can make long-term investments in capital and talent. Some contracted services have been fiscally efficient and effective. Others have been medically effective but not cost efficient. Finally, some have been less than satisfactory in point of both cost and productivity.

In 1976 the National Academy of Sciences (NAS) studied the VA health-care system and found it deteriorating. NAS proposed that either the VA cease its health-care functions or, alternatively, that emphasis be given to better funding and management so that the VA could provide veterans with care at the standards which have been achieved by the medical arts and sciences and which are available in other health-care systems and facilities.

NAS specifically studied the VA prosthetics program. Following World War II the VA assumed a role of leadership in prosthetics, and it earned an international reputation for excellence through its research, development, and clinical application in the field. The National Academy of Sciences found in 1976, however, that this excellence had disappeared.

There are three reasons noted by the NAS study for this loss of excellence in prosthetics: insufficient appropriations, fragmentation of VA managerial control, and increased independence of private contractors.

The VA provided the foundation for private contractors to build upon and improve the whole area of prosthetics, and the VA has continued to serve contractors as a reliable major buyer of products. But, contractors' failure to achieve high

standards on a consistent basis is well-attested. Employers have failed to supervise their workers and the VA must pay more—first the VA purchases the devices only to have to pay the supplier to rectify defects arising from shoddy workmanship. Of more direct importance to the well-being of severely disabled veterans is the fact that these contractors have shown little or no creativity, largely because research and development would reduce their profits.

This failure to advance in the field of prosthetics has come even though the VA has maintained skilled personnel to oversee the program, and PVA shudders to think what the result would be if contractors were not monitored by VA supervisors and specialists.

Recently the House Committee on Veterans' Affairs conducted hearings on the likely effects that greater contracting will have on the VA health-care system. One week later, on October 27, 1981, the Honorable Ronald Mottl introduced legislation (H.R. 4851) "to amend title 38, United States Code, to exempt the Department of Medicine and Surgery in the Veterans' Administration from any Office of Management and Budget policy or directive prescribing procedures for contracting-out commercial or industrial functions."

Non-VA hospital administrators, health-care professionals, hospital employees, and suppliers of goods and services testified at the hearing, and the great preponderance of them illustrated the problems they have faced and the harm which has resulted to patients when medical systems have relied on contractors for services such as hospital housekeeping services, food preparation and delivery, and linen services.

PVA will not reiterate the examples given during the hearing, but these knowledgeable witnesses reported that too often various hospitals have found themselves paying considerably more for sub-standard sanitation levels, cold and/or improperly prepared food, and shortages of clean linen. Concededly opponents of contracting can provide an infinite number of bizarre stories to illustrate where contracting has failed, just as supporters of the provisions of A-76 can offer an equal number of examples to illustrate that contractors would provide services more cheaply than do VA employees. But, one does not have to be a sophist to argue that the preponderance of the evidence detracts from the viability of imposing the provisions of Circular A-76 on the VA's Department of Medicine and Surgery.

A procurement and supply expert from the Veterans Administration testified before the House Committee on Veterans' Affairs, and he pointed out that the VA already relies on contractors, but all such decisions "should be based on considerations other than just cost factors, such as the availability of satisfactory service and the relative isolation of many of our facilities with the concomitant nonavailability or limited availability of prompt services to maintain critical operations." OMB seems to be considering just cost and ignoring the needs of local VA facilities and particular hospital patients.

In addition to harming veterans health and medical care by making blanket demands without considering the needs of individual facilities, programs, and patients, PVA sees in Circular A-76 other inevitable harms which are likely to arise, should the VA's Department of Medicine and Surgery comply with the Circular.

First, the OMB Circular would undermine hospital administrators' control over their facilities and personnel. Contract personnel answer to their employers and not to the parties having work done. Whenever problems arise the administrators would have to consult with the contractor who either would consult with employees' labor union representative or the employee, depending on whether or not workers are unionized. Here would be needless delay and aggravation for managers and, meanwhile, hospital patients would suffer. Second, contractors' employees may be unionized and can strike. In the event of strikes either patients' needs would not be met or health-care professionals and managers would have to perform contract functions. (The AFL-CIO has opposed A-76, and Congress recognized through Public Law 96-330 that health-care professionals are already overworked.) Either of the possibilities noted are unsuitable: patients are in hospitals for the obvious reason that they are not well, and it is asking a great deal of a sick person to wait until food or linen or medications can be found. Labor strikes occur most often when workers are forming their bargaining units and soon after employers restructure and/or expand their operations. Strikes also occur when labor agreements are being re-negotiated.

It is anticipated that contractors will attempt to accomplish their tasks with fewer employees than the VA uses, because reducing labor costs is a major way to increase the employer's profits. Under these circumstances several possibilities exist: the services would be provided less completely and more slowly; contractors would hire additional workers and increase their charges to the VA; contractors employees will continue to be overworked, will feel beleaguered, and will conduct unfair labor practice strikes. Again, hospital patients suffer.

Third, employees of contractors work only as hired help and not as members of a team. Unlike VA employees, they are not likely to have much interest in the VA health-care system outside their particular assignment areas. For them it probably would not make much difference whether they were cleaning linen for hospital patients or for a barber shop, or preparing food for sick people or airline lunches—the same contract employee would likely work on VA and non-VA assignments within the same day or week.

Fourth, even if a provider's period of contract functioned smoothly, the contract must be reviewed upon expiration. The President of Huntington Laboratories, Inc., a for-profit manufacturer and seller of institutional housekeeping products, recently reported on his observations of such events: the hospital must accept the contractor's renewal terms or be without services, and each contract renewal is tantamount to a strike. The hospital must "magically produce—instantly—a fully trained staff" to fill the void, and such a staff would not exist should the provisions of Circular A-76 be implemented in the VA's Department of Medicine and Surgery.

As noted, PVA wants to consider both the quality of health care and the cost of it. The factors previously mentioned would undermine the quality of VA care, should the provisions of Circular A-76 be implemented.

Cost effectiveness itself speaks against increased reliance on contractors as envisioned by proponents of Circular A-76. On October 8, 1981, Stars and Stripes published what it described as an analysis of a confidential OMB memo. The memo outlines budget reductions sought by the Administration in the VA's budget for Fiscal Years 1982, 1983, and 1984. PVA considers the information concerning

proposed future reductions to be reported accurately, in part, because the ones noted for FY 82 were sought by the President and OMB during budget considerations earlier this year.

It should be emphasized at this time that one of the Administration's goals reported in Stars and Stripes is to eliminate 3,844 employees from the Va Canteen Service, but contracting out will cost \$1,793,000 more in FY 83 and \$1,915,000 more in FY 84. PVA recognizes that the ultimate goal behind such a measure is to realize long-term savings by not having to pay these employees retirement benefits. And, canteen services are not as urgent a need for hospital patients as some of the areas covered by Circular A-76. But, there are anticipated increases in contract costs, and Congress cannot control these increases as directly as it can VA employee pay raises. Also, the greater cost of contracting will be felt immediately, a fact which will consume the funds which Congress regularly provides for veterans health and medical services.

The Honorable Tom Harkin (D-Iowa) stated recently, in opposition to applying Circular A-76 to the VA health-care system, that historically once such contracts are in place the rate of increase is approximately 25 percent between the first and second years. He added that "without a test program, there is no justification for saying that contracting out will save money."

OMB is in the budgeting business, and it does not consist of health-care experts. And, even in budgeting matters we should monitor closely OMB's policies which so directly affect veterans health. In rushing toward greater contracting the Air Force Academy experienced some adverse results when its statement of work

greatly underestimated the contractor's assignments. As a result, the three-year contract price had to be increased by about \$708,000. PVA wonders if OMB, in setting guidelines for the VA, has considered the cost of such time-consuming tasks as preparing specialized meals for patients on controlled diets. It is fortunate that the events at the Air Force Academy concerned only the cleaning of floors in the field house and similar buildings.

Should the provisions of A-76 be implemented in the VA, the results will be virtually irreversible, because the VA will have dismantled much of its operation. And, A-76 seems to prohibit bringing back in-house services unless there is a 10 percent savings in personnel costs and a 25 percent savings in capital equipment. The VA could not easily meet these requirements since it would have to begin a rebuilding process.

During the past few Administrations, and now during this one, OMB has sought to destroy the VA as a viable, independent health-care provider for veterans. The assaults have not been for purely economic reasons and distinguished Members of this Committee have worked to thwart the destruction of the VA. PVA remains forever grateful for your loyal support, and we understand that even though you have consistently led the entire Congress to appropriate needed funds for the VA, OMB has at times withheld those health-care funds.

The VA's General Counsel has ruled that the provisions of Circular A-76 do not violate the provisions of Title 38, United States Code, so long as contracting out direct patient care is precluded. PVA maintains that perhaps the Circular does not violate the law, but this is an overly legalistic interpretation of the law as it

affects the well-being of veterans who are patients in VA hospitals. Timely admissions for treatment, proper medications, appropriate diet, and sanitary conditions are as much a part of recovery for patients as is skilled surgical procedures and trained nursing care. And, the professionals who provide these latter services will find working conditions even more difficult when the previous services are inadequate.

PVA requests the Members of this Committee to introduce legislation such as H.R. 4851, introduced by Representative Mottl. If, after more adequate study, Congress decides at a later date to implement provisions such as those contained in A-76, the amendment to Title 38 could be repealed. On the other hand, if OMB is allowed to continue with the provisions of the Circular, the effects will be irreversible. PVA supports such an important decision being made by Congress and not by the Office of Management and Budget.

In conclusion, there are some additional points worth mentioning and of special importance to those who represent individual communities. For example, A-76 does not require a socio-economic impact statement: as Representative Harkin notes, in a community in his District 316 jobs will be lost in a town of 8,000 people, should A-76 be implemented in the VA's health-care system. In all, 22,800 employees will be dismissed from employment, many at the later stages of their careers. Of this number 64 percent (15,592) are veterans who served the Nation and have made careers of serving veterans. PVA doubts that contractors' employees will work as diligently under VA conditions for as little pay as have these individuals.

Mr. Chairman and Members of the Committee, this concludes my statement and I will be glad to answer any questions that I can.

Chairman SIMPSON. We have a bit of a change in the order of this next group of witnesses. I will first hear from Mr. Charles Wicks, the president of the National Association of Government Employees, Local R-4-78 in Martinsburg, W. Va. Then we will hear from the panel of AFGE witnesses headed by Kenneth Blaylock, the national president, and Mr. Daniel Kearney of the organization.

Mr. Wicks, if you will join us. I have a rollcall vote and I will probably have to leave before 5 minutes. Hopefully, I will hear your testimony. I will then leave the staff director to ask a question or two, and then I will return for the other members. So please, sir, go ahead.

TESTIMONY OF CHARLES WICKS, PRESIDENT, NATIONAL ASSOCIATION OF GOVERNMENT EMPLOYEES, LOCAL R-4-78, MARTINSBURG, W. VA.

Mr. Wicks. Mr. Chairman, I want to thank you for the opportunity of allowing me to present our views. I am Charles Wicks. I am employed at the VA Medical Center at Martinsburg, W. Va., as a biomedical engineering technician. I am also president of local R-4-78 of the National Association of Government Employees.

I would like to first bring to the attention of the committee the relationship between the employee and the patients. Most of our employees of Martinsburg are veterans, and I believe that because of this the patient receives extra care. There is a good understanding, a rapport, and because of dedication and loyalty of the employee they assist the patient in many ways that they are not required to.

One of the ways is that they often help the patient by taking him out to various dinners and stuff. They also help the family. You have to understand that we are a small community and pretty well knit.

Many patients have expressed preference of not having nonveteran employees taking care of them. They are concerned, the patients are concerned because of their possible disfiguration and other abnormalities that often patients have, that they would not receive the same consideration from nonveteran employees.

If the contracts do go into effect they feel that younger, possibly even teenagers might perform this type of work, and this they would not feel comfortable with. The veteran patient expresses a strong desire to have veterans, or at least adults, understanding adults take care of them.

The impact of A-76 at our station in Martinsburg is rather dramatic. Last August the director called the dietetic employees together and explained the possibility of this service being contracted out. The immediate effect was panic, the employees feeling betrayed, and many of the employees called me at home at night crying on the phone, not knowing what to do.

A lot of the employee households have been reduced by one income because of the local job market, General Motors, Corning Glass, Mack Trucks have been laying off employees and are continuing to lay off. If the contract does go through these employees have been told that the wage they now receive will probably be

dropped dramatically in the neighborhood of minimum wage and that they could not afford to keep their present homes or the present standard of living. They feel a feeling of hopelessness in that they would be dependent on public assistance.

I believe that the present Veterans' Administration policy of predominantly having patients, veteran patients taken care of by veteran employees is the best policy, that the Veterans' Administration does use contracts when it is advantageous to the service.

I do thank you.

Mr. HARVEY [presiding]. Mr. Wicks, I am sorry that Senator Simpson had to excuse himself for that rollcall vote. Your spoken comments this morning will of course be transcribed by the reporter and entered in the record.

Senator Simpson said that he will be back in just a few moments. I propose that we take a very brief recess until his return from this rollcall vote occurring on the floor of the Senate. Thank you.

[Brief recess.]

[Hearing resumed.]

Chairman SIMPSON [presiding]. Thank you so much for your understanding of the rollcall vote situation.

We now have the pleasure to welcome Mr. Kenneth Blaylock, president of the American Federation of Government Employees, Washington, D.C., and Mr. Daniel Kearney, national vice president of the first district of the AFGE of Canton, Mass. Mr. Kearney will be accompanied by Nelson Hunt of the Jamaica Plains VA Medical Center, and Patricia Warren of the VAMC at White River Junction, Vt.

Let me read into the record rather than present it the note from my good colleague Ted Kennedy who says,

Dear Chairman Simpson. I hope to attend your hearing this morning on OMB Circular A-76 but I am not able to due to previous commitments. However, I did want you to know of my interest in the testimony of Daniel Kearney, National Vice President of the American Federation of Government Employees. Dan's leadership in that union has meant a great deal to Government employees across our Nation. I know you will give special attention to his remarks. Sincerely, Ted.

That will be part of the record.

With that, we appreciate hearing your testimony.

TESTIMONY OF A PANEL OF REPRESENTATIVES OF THE AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES CONSISTING OF KENNETH T. BLAYLOCK, PRESIDENT, AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, WASHINGTON, D.C., ACCOMPANIED BY BILL ROLLINS, PRESIDENT, AFGE LOCAL 2610, VA HOSPITAL, TOGUS, MAINE AND PAT WARREN, PRESIDENT, AFGE LOCAL 2604, VA HOSPITAL, WHITE RIVER JUNCTION, VT.; AND DANIEL J. KEARNEY, NATIONAL VICE PRESIDENT, FIRST DISTRICT, AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, CANTON, MASS., ACCOMPANIED BY NELSON HUNT, PRESIDENT, AFGE LOCAL 2143, VA HOSPITAL, JAMAICA PLAINS, MASS. AND DON HAINES, LEGISLATIVE ASSISTANT

Mr. BLAYLOCK. Thank you very much, Senator. I also have this morning Bill Rollins from Local 2610 and Pat Warren from our Local 2604 VA hospital. And with us at the table this morning,

Don Haines, who is one of our legislative assistants who has worked extensively on the issue of contracting out.

We are pleased this morning, Senator, that you have given us an opportunity to testify on contracting out. I have a 16-page statement with attachments I would like to introduce for the record, and I have a brief summary that I will give orally. Then we will be glad to answer questions.

Chairman SIMPSON. Thank you. The full statement will be accepted into the record.

Mr. BLAYLOCK. There is probably no area in Government that has more lofty sounding principles and more shoddy practices than contracting out. The Office of Management and Budget has demonstrated a consistent bias in favor of contracting out regardless of the cost to Government or the sacrificing of quality in many cases of service to the taxpayer and in this case to the veterans who are patients in VA hospitals.

We have no objection to the general principle that the Government should rely on private industry to supply products. We do not believe the Government should be in the manufacturing business. The Government should buy planes, not make them.

Securing services, however, is a different matter. The purpose of Government is to provide necessary services to the people. We don't think that Government should surrender its function and responsibility to private business.

We agree that A-76's lofty principle is that Government should not compete with its citizens. We agree with this principle. But continuing to have VA hospital work done in-house does not compete with private citizens because the in-house work is the business of Government and not that of private contractors.

For example, when a VA medical center has some linen, patients' clothing and whatever to launder, it is under no greater obligation than Ms. Murphy is to send it down to the corner laundry. It would of course be a different matter if the medical center suddenly started soliciting the business of patrons of the corner laundry. Then we would have a genuine example of Government competing with private industry.

Even if one agrees as a matter of policy that in general Government should rely on outside contractors for both its goods and its services, one has to admit that A-76 is biased in favor of that policy. This bias toward contracting out interferes with other principles, some of which even receive lip service from OMB.

Circular A-76 says that so-called inherent Government functions should not be contracted out, yet there is a total lack of a comprehensive, understandable, usable definition of what is an inherent Government function and how you make that determination.

Before this attempt by OMB to force the VA to implement A-76 we would have thought that medical and hospital care for veterans of our armed services suffering injuries sustained in the defense of our country would be a prime example of an inherent Government responsibility and function. Obviously OMB sees a much stricter limit to that definition.

The delivery of medical and other hospital assistance, together with rehabilitative services to veterans, is really part of the Government's continuing responsibility for national security. Veterans

only come from one activity, service in the Armed Forces of the United States of America. If there is any activity of Government that meets the test of inherent Government responsibility and inherent governmental function it is the responsibility of direct patient care and those support functions of indirect patient care that have a direct impact on the quality of medical care provided to veterans.

OMB and the contractor lobbyists, however, have displayed no such sensitivity to the Government responsibility. On pages 5 and 6 of my prepared statement I note how OMB's calloused contracting out in DOD so raised a concern over jeopardizing our national defense that the Congress itself was forced to enact legislation controlling and restricting contracting out.

A-76's lip service to inherent Government function is mirrored by its references to cost comparisons. It is so biased that it forces contracting out even when it is more cost effective to perform the functions in-house. And there are examples of that.

A-76, for example, contains no meaningful requirement that contractors meet the same job requirements that are currently being performed by Federal personnel. Without this, the contractor can easily underbid by lowering the level of performance or level of care. In VA hospitals, of course, of the VA system, this would be a calamity.

On pages 7 and 8 of my statement I note how VA followed this practice of allowing a drastic cut in service by the way that it wrote up the prototype statements of work for dietetic services. Their prototype fails to make any provisions for special diets. And you all know that special diets is a part of the actual treatment and therapy for patients. These special diets are often required for a majority of hospital patients and are a major element of patient treatment and care. They require individual preparation. Yet VA failed to include them in their prototype statements of work.

A-76 also inflates the in-house cost estimate and thereby misses an opportunity to make Government more efficient and more cost effective. Pages 8 and 10 of my statement discuss several ways in which A-76 overestimates the in-house cost including inflated retirement expenses, inflated procurement costs, and unnecessary bureaucracy and overhead structures.

Consistent with its bias, A-76 also underestimates the cost of performance by outside contractors. If it were serious about comparing total costs it would add the expense of cost studies and of processing a reduction in force to the contractor's prices, because no contract could be let without these costs.

On pages 10 through 13 of my statement I note other ways in which A-76 favors the private contractor and ignores a true competitive system. I do not subscribe to the idea that private business is automatically more efficient than Government. If that would be the case then maybe Congress' role would be to simply establish one large procurement agency and we contract out all of Government.

With that, Senator, we have a series of recommendations that is in my full statement. It is there for your consideration. We will be glad to answer questions on it. Mr. Kearney has a short 2-minute statement or so.

Chairman SIMPSON. Thank you very much, Mr. Blaylock.

[The prepared statement of Kenneth T. Blaylock, national president, American Federation of Government Employees, and the American Federation of Government Employees' response to written questions submitted by Hon. Alan Cranston, ranking minority member of the Senate Committee on Veterans' Affairs, follow:]

AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES

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AMERA

PREPARED

STATEMENT OF

KENNETH T. BLAYLOCK
NATIONAL PRESIDENT

AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES

BEFORE

COMMITTEE ON VETERANS' AFFAIRS
UNITED STATES SENATE

ON

OMB CIRCULAR A-76
AND CONTRACTING-OUT IN THE VETERANS ADMINISTRATION

NOVEMBER 5, 1981

The American Federation of Government Employees, AFL-CIO, is pleased to have the opportunity to appear and testify before the Senate Committee on Veterans' Affairs. AFGE represents over 700,000 personnel throughout the Executive Branch of government, and is the exclusive representative for approximately 110,000 employees in the Veterans Administration for purposes of collective bargaining under Title VII of the Civil Service Reform Act of 1978.

Let me say at the outset that we are very pleased that hearings have been scheduled to examine the problems associated with contracting-out practices in the Veterans Administration. We believe

that the recent contracting-out offensive ordered by the Office of Management and Budget represents a very real threat to the integrity of the VA health care delivery system.

Today, we would like to focus our remarks on OMB's track record in trying to force the Executive Branch to expand the use of private contractors without proper regard for cost-effectiveness, quality of work, inherently governmental functions, or efficiency and productivity in government. We would then like to make some suggestions for how Congress should address contracting-out in the Veterans Administration.

OMB AND ITS CIRCULAR A-76 ARE OPENLY BIASED IN FAVOR OF CONTRACTING OUT

OMB Circular A-76 contains a built-in bias in favor of contracting out government work. The contractor lobbyists worked hard to ensure this bias. In addition to this structural bias, A-76 has been consistently implemented by OMB and other agencies so as to favor contracting out.

In issuing Circular A-76, the Office of Management and Budget was in part quite candid in admitting its bias in favor of contracting out. OMB's Bulletin 81-15 on A-76 declared that it was the Administration's general policy to rely on "private enterprise to supply the products and services the Government needs."^{1/}

^{1/} Paragraph 4 of OMB Bulletin 81-5, reprinted at page 93 of the Hearing on VA Implementation of OMB Circular A-76, Policies for Acquiring Commercial or Industrial Products or Services, Before the House Veterans' Affairs Subcommittee on Oversight and Investigations, 97th Cong., 1st Session. (July 14, 1981) (Serial No. 97-31). References to documents and page numbers are taken from the July hearing except where noted otherwise.

AFGE has no objection to the Government relying on private industry to supply products. We do not believe Government should be in the manufacturing business. The Government should buy planes, not make them. Securing services, however, is a different matter. The purpose of Government is to provide necessary services to the people. Government should not surrender its functions to private business. OMB's Bulletin further proclaims that "the Government should not compete with its citizens."^{2/} AFGE agrees with this concept, but we recognize that the statement is more an appeal to emotion and not to logic.

Continuing to have VA hospital work done in-house does not "compete" with private citizens, because the in-house work is the business of the Government and not that of private contractors. For example, when a VA Medical Center has some linen and patients clothing to launder, it is under no greater obligation than Mrs. Murphy to send it to the corner laundry. (It would, of course, be a different matter if the Medical Center suddenly started soliciting the business patrons of the corner laundry. That would be a genuine example of Government competing with private industry. We know of no such action by any Medical Center laundry.)

Even if one agrees, as a matter of policy, that in general Government should rely on outside contractors for both its goods and services, one has to admit that A-76 is biased in favor of that policy.

^{2/} Paragraph 4 of OMB Bulletin 81-5, reprinted at page 93.

In determining whether that policy is wise in practice, we have to examine A-76 to see how this policy is implemented in conjunction with other principles--such as containing the cost of Government care for veteran patients maintaining, the control and quality of the workforce by Government managers, and preserving Governmental functions. To be fair and balanced, A-76 should take all these factors into proper account. Unfortunately, it does not. As a result, A-76 amounts to little more than blind, unyielding prejudice against performance of Government work by Government employees. For the VA hospital system this prejudice would be disastrous.

A-76 ALLOWS CONTRACTING OUT OF GOVERNMENTAL FUNCTIONS

Circular A-76 refers to some functions as "inherently governmental" and says that these functions must be performed by Federal personnel.^{3/} AFGE couldn't agree more. Unfortunately, the circular fails to provide a usable and comprehensive definition of what is inherently governmental.

Before this attempt by OMB to force the VA to implement A-76, we would have thought that medical and hospital care for veterans of our armed services, suffering injuries sustained in the defense of our country, would be a prime example of an "inherently governmental" function. Obviously, OMB sees a much stricter limit on that definition.

^{3/} Paragraph 4b of OMB Circular A-76, reprinted at page 30.

The delivery of medical and other hospital assistance, together with rehabilitative services, to veterans is really a part of the Government's continuing responsibility for national security. Veterans only come from one activity--service in the armed forces of the United States of America. If there is any activity of Government that meets the test of an inherently governmental function, it is the responsibility of direct patient care and those support functions (like food services, laundry and housecleaning) that have a direct impact of the quality of medical care provided to veterans.

OMB and the contractor lobbyists, however, have displayed no such sensitivity to government responsibilities.

One would assume that national defense is one "inherently governmental" function, and, indeed A-76 contains several references to national defense.^{4/} In practice, however, A-76 contracting out so adversely affected the Department of Defense, that the House Armed Service Committee was compelled to recommend statutory restrictions on DoD's contracting out. In 1979, Congress enacted those restrictions for a one-year period and made them permanent law a year later.^{5/}

During this session the Armed Services Committee recommended tightening the law to require a certification that contracting out would not adversely affect mobilization readiness, emergency

^{4/} See paragraphs 5f(1) and 8b of OMB Circular A-76, reprinted at 30 and 35.

^{5/} See section 806 of Public Law 96-107 and section 502 of Public Law 96-342.

contingency missions, or anticipated requirements in the event of a war. For all the references to national defense, OMB and the contractor lobbyists opposed the Armed Services Committee's attempt to safeguard defense in 1979, in 1980, and again this year. We believe that this also reflects OMB's prejudice against in-house performance.

A-76 FORCES CONTRACTING OUT REGARDLESS OF COST EFFECTIVENESS

A-76's lip-service to "inherently governmental" functions is mirrored by its references to cost comparisons.

The March 29, 1979 memorandum for A-76 to the agencies provides that "relative cost must be given appropriate consideration in decisions between in-house performance and reliance on private commercial sources.^{6/} Defenders of A-76 like to pretend that this means that cost-effectiveness governs the choice between performance in-house and by contractors. Even if lower cost were an appropriate sole criterion governing hospital care for veterans--and we believe it is not--the OMB Circular in fact makes no real effort to have genuine cost comparisons. Once again, A-76's bias in favor of contracting out almost completely undercuts other governmental interests, like decreasing costs where feasible.

At the heart of any genuine cost comparison is the statement of work. Unless the agency requires the contractor to meet the same job requirements that are currently performed by Federal personnel,

^{6/} Paragraph 2 of OMB Circular A-76, reprinted at page 29.

the contractor can easily "underbid" by lowering the level of care. In the VA hospital system, of course, this would be a calamity.

For example, requiring hospital areas to be cleaned twice-a-week instead of every day obviously increases the risk of contamination and infection to patients. But it would provide a "savings." If that standard is really acceptable, however, then the in-house costs should be based on twice-a-week service also. In most cases, of course, budget shortages have already required VA employees to perform so many different tasks that the actual work requirements of each task have been reduced to the minimal level acceptable. In some cases, VA has been forced to reduce care below medically acceptable standards. If twice-a-week cleaning were tolerable, it would already be applied in-house, so that some of those cleaning employees would be free to do other duties.

Incomplete and inaccurate statements of work have frequently been cited by the General Accounting Office as a prime area of abuse in contracting out.

VA itself also fails to require precise statements of work for the services to be contracted out. The latest prototype statement of work for hospital services contains only minimal requirements. In areas like dietetic services the VA obviously cannot be satisfied with allowing the contractor to perform just minimal requirements. For example, the VA's prototype statement of work fails to make any provision for special diets such as those involving diabetic prescriptions. These "special diets" are often required for a

majority of hospital patients and are a major element of patient treatment and care. They require individual preparation. Yet, the VA has failed to include them in their prototype statements of work. Contractors will benefit from VA's failure by being able to lower their costs and their service.

What patients and employees obviously need, however, is legislation in which Congress imposes on the agency a real requirement that statements of work be accurate and complete. That legislation should also guarantee line managers and employees, through their representative, both access to the information and meaningful involvement in writing the statements of work. A-76 fails to contain these safeguards.

The Circular should also require regular and accurate accountability to Congress and to the Congressional committees which exercise jurisdiction. OMB, VA, and the contractors are not accountable to the American people--but you gentlemen are.

A-76 INFLATES THE IN-HOUSE COST ESTIMATE

Another reflection of A-76's prejudice against performance by government personnel is its conspicuous failure to require that the in-house cost estimate be based on the most efficient organization and staffing. In practice, GAO has found that cost estimates are based on current staffing and organizational patterns, thereby penalizing Veterans and other Federal employees for what may be needless layers of managerial bureaucracy and excess overhead costs.

For example, in-house estimates often are based on the needlessly

complicated and expensive procurement systems of the General Services Administration or the Defense Logistics Agency. GSA's mark-up, for example, is 21% of the wholesale price to GSA of the procured materials. A contractor, on the other hand, can just shop down at the local wholesaler. It is hardly fair to punish the VA employees because OMB imposes a fixed 21% markup for goods ordered through GSA.

The House Armed Services Committee was so dismayed at this practice of simply rubberstamping the agency's current organizational and staffing practices, that the DoD statute enacted into law by Congress requires that the cost comparison be based on "the most efficient and cost effective organization" of the function to be contracted out. This requirement ensures that any cost savings will be genuine and not an illusion designed simply to guarantee contracting out. OMB and the contractor lobbyists, however, adamantly opposed this requirement.

We think Congress has an opportunity to use the competitive bid process to accomplish a goal you all share--namely, bringing about a more effective and efficient Government workforce. But this opportunity can only be taken if you require that the cost comparison be based on the most efficient in-house organization.

OMB Circular A-76 also inflates the cost of in-house operations by arbitrarily adding on 20.4% as a figure for retirement costs including the so-called "unfunded liability." This figure is sheer guesswork; OMB has never established its validity. It is more than

three times the figure (7%) used in earlier versions of A-76. OMB has never required that the unfunded liability of the Social Security system, which is used by contract employees, be added to the contractor's cost. Nor does A-76 impose any estimate of the eventual welfare costs to the government when contract employees, whose employer provided no pension plan, finally retire.

In fact, A-76's treatment of retirement is an excellent example of how biased it is in favor of contracting out. Although guesswork, the 20.4% figure for in-house retirement costs is in theory based on the total, "dynamic" cost to the government of the civil service retirement system. This in effect forces the in-house cost estimate to include the cost of retirement over a thirty-year period while the contractor's cost estimate is based solely on his outlays for the period of the contract. Legislation is needed to require that the in-house costs and contractor costs cover the same period.

Actuarial modeling is commonly used in structuring insurance and retirement programs, but its results are often vague and subject to necessary corrections and re-corrections. Actuarial modeling, however, has no valid application to the competitive bid process. This is especially true when it is only applied to one side. The comparison should be between the actual costs for the period of contract only.

A-76 ALSO FAVORS CONTRACTING-OUT IN OTHER WAYS

If A-76 were serious about the relative cost of performance by Federal personnel versus contracting out, it would also require that

the expense of the cost studies and processing a reduction-in-force be added to the contractor's prices because no contract could be let without these costs. The A-76 cost comparison handbook also, in effect, arbitrarily lops 40% off the actual cost of severance pay, homeowner's assistance, pay rate retention, relocation and retraining expenses, and the physical inventory required to implement the contracting out by requiring that the comparison be based on only three-fifths of the costs. Once again, OMB thereby deflated the cost estimate for the contractor.

If cost-effectiveness were a genuine goal of the circular, A-76 would bar the kind of increases in contract price that are now routinely given contractors in succeeding years or, even in the initial year when the statement of work has to be corrected. Fewer contracts with escalator clauses should be allowed. Rather, close-quoted contracts should become the norm.

Another effective check on escalating contract prices would be an absolute requirement that an agency retain a core in-house capability or a specific requirement to maintain such capability. As a result, operating managers at the local level must accept a contractor's increased costs, whether fair or not. These problems existed before A-76, and it is unlikely that the failure to address them was accidental. VA, of all places, needs legislation that, at least, requires the retention of core capability.

Once an agency function is contracted out, A-76 prohibits it from being brought back in-house unless there is 10% savings in

personnel costs and a 25% savings in capital equipment. Once again, A-76's supposed emphasis on cost effectiveness gives way to its bias in favoring of contracting out functions and keeping them out.

Moreover, once a contract has been awarded to a small business concern, A-76 provides that it will not be reviewed for conversion to in-house performance. This has led to unfortunate circumstances where the small business defaults or is otherwise unable to perform the service, but the Government is denied the opportunity to ascertain whether in-house performance would now be cheaper.

Legislation is needed in order to require rigid evaluation of performance and costs so that all functions performed by contract employees will be reviewed for reconversion to in-house performance---just as in-house functions are reviewed for conversion to contract.

The most important bias in A-76 towards contracting out is that it contains no effective provisions for enforcement, even of its own biased requirements. Time and again, AFGE has sought to enforce A-76's own language in court only to be met by OMB's objection that the circular has no force of law or regulation. (When ordering VA to comply, however, OMB doesn't say A-76 is only advisory.) In addition, OMB argues that decisions by agency heads under A-76 cannot be challenged. Even if challenges were allowed, the circular lacks both specific standards that are precise enough to serve as the basis for review and any requirement that affected parties can avail themselves of information which only the agency possesses. Legislation

is obviously required to meet these needs.

All of these deficiencies yield the conclusion that no one can honestly say that private sector is in fact more cost-effective than in-house performance for performing the same scope of work and level of care.

VA REQUIRES SPECIAL STANDARDS FOR CONTRACTING OUT

We have focused our testimony on the various ways in which OMB Circular A-76 is biased, both in policy and in practice, towards contracting out. We have pointed out how A-76 does not even live up to its own minimal standards of fostering cost-effectiveness. We would not want, however, to leave the Committee with the impression that AFGE believes cost-effectiveness should govern contracting out in the Veterans Administration. A single-minded focus on cost-effectiveness, even if implemented fairly, would destroy other principles which are especially important in the Veterans Administration. These principles now require legislative protection.

AFGE urges that this Committee report out legislation which will:

- (1) prevent medical care and other benefits for veterans of the armed services from being sacrificed either by direct budget cuts or through the guise of contracting out;
- (2) prevent the contracting out of either direct or indirect patient care;
- (3) prevent the effects of veterans preference from being diluted through contracting out;
- (4) preserve the control of Government managers over the entire VA workforce, in-house and contract;

- (5) preserve the stability in the VA workforce which Federal personnel now provide;
- (6) ensure that any contracting out permitted under the above standards also meets rigid cost-effectiveness requirements, including accurate and complete statements of work and the most efficient in-house organization and staffing;
- (7) ensure that the statutory requirements will be fully enforceable and not subject to bias in favor of contracting out; and
- (8) ensure that complete records on the cost performance and size of the contract workforce will be collected and available in a central location.

Although we have focused on the bias in OMB Circular A-76, no one should forget that the VA has already engaged in contracting out by using its own authority under title 38 of the United States Code. And, as might be expected, many of the same problems arose. Incomplete and inaccurate statements of work, greater costs, inadequate service, and destruction of in-house capability have already occurred. We have submitted for the record two statements by AFGE officials from the Veterans Administration. Their statements point out the problems contracting out is already causing in the VA.

I want to note that the VA's contracting out places VA medical services at the risk of possible strikes by contract employees seeking better working conditions from the outside contractor. It's perfectly legal for contract employees to strike, and the fact that so many contractors are not organized increases the likelihood of strikes. Many studies have shown that the most likely time for a strike is when employees first set up a union and negotiate their first contract. Federal employees, of course, are barred by

law from striking. More important than legal prohibitions, is the dedication of VA employees to their work--dedication that now causes them to report to the hospital during blizzards and power outages in order to be available just in case they are needed.

An increase in contracting out at VA would also raise the possibility of graft and corruption. The employee-manager relationship in a Government agency provides almost no opportunity for corruption. The large sums involved in letting contracts, however, and the intrusion of the profit motive present the opportunity for graft when contracting out gets underway. It would sadden me to think that any of the scarce funds available for vital VA programs would be wasted through graft and corruption. Frankly, it is a scandal that after years of Congressional questioning OMB still cannot answer how many contract employees are in the Government's "invisible workforce" and how much money the taxpayer spends on that workforce. No agency would ever dare be so cavalier with its own personnel appropriations.

I do not subscribe to the idea that private business is automatically more efficient than Government. Such a general conclusion is simply not supported by experience or fact.

But even if it were an automatic fact, the procedure under Circular A-76 for letting a service contract with its failure to monitor or enforce that contract, eliminates the very elements of competition that would make private enterprise more efficient. A-76 contracts are open-ended, have escalator clauses, are paid on a cost-plus

basis with automatic renewals. Moreover, once that work is performed on contract and the in-house capability destroyed, the contractor enjoys a monopoly situation. In fact, it is exactly the rules of free enterprise that predict what will happen with such a monopoly.

I want to thank you for the opportunity to appear before this Committee and pledge AFGE's continued support in your efforts to guarantee that the Veterans Administration provides quality care and benefits to the Veterans of America's armed forces. We also appreciate the work of this Committee on Public Law 97-66 which ensures that Congress will have the time to address these problems legislatively.

RESPONSE OF THE AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES TO WRITTEN QUESTIONS
SUBMITTED BY HON. ALAN CRANSTON, RANKING MINORITY MEMBER OF THE SENATE
COMMITTEE ON VETERANS' AFFAIRS

QUESTION 1 (A). Have there been a substantial number of cases in which employees represented by AFGE have been displaced by A-76 contractors?

AFGE RESPONSE. Literally thousands of employees represented by AFGE have been displaced by A-76 contractors. Our experience indicates that this displacement occurs in two waves. Frequently, a large number of employees lose their jobs when their work is first converted to contractor performance. Contractors often change the composition of the workforce and then deny (often incorrectly, we believe) that employees meet the qualifications to perform the old work under the recrafted job classifications. Other employees are displaced because they cannot make the economic adjustments in pay or benefits required in order to accept a position with the contractor. This latter situation particularly occurs when a contractor chooses to run a "meat market" operation, paying only the minimum wage and relying on transient labor, with little concern for continuing quality of work.

The second wave of displacements occurs after the initial conversion to contractor performance. In some instances, this results from a change from one contractor to another. In other cases successor contractors frequently engage in various ruses in order to displace employees. In other situations, employees are displaced because they are unable to continue working under the contractor's terms and conditions of employment.

AFGE is prevented from making a more quantitative response by the general refusal of agencies to provide us with information about development after the contract is granted. We have consistently requested and been refused information about employee placement, contractor performance, cost overruns, and contractor bankruptcies.

AFGE has also urged the establishment of a central depository for complete information on contracting out. The failure to establish such a source of information also makes impossible a complete answer to these questions.

QUESTION 1 (B). What has been your assessment of the extent and success of the efforts made by the agencies concerned in helping the displaced employees get comparable jobs with the contractor or elsewhere in the agency?

AFGE RESPONSE. Our experience is that agencies generally limit their efforts to secure employment of displaced employees by the contractor to reminding the contractor that they are theoretically required by OMB Circular A-76 to offer jobs to these employees. The agencies, in other words, make no general effort to ensure that employees are actually placed or that a change in proper qualifications has not been used to arbitrarily bar continued employment for the displaced workers.

Our experience also indicates that agencies frequently make little effort to secure placement of displaced employees within the agency, although this is sometimes done.

Once again, the refusal of agencies to provide post-contract information and the failure to establish an informational clearinghouse

on contracting out prevents us from making a more detailed response.

QUESTION 2. What has been AFGE's reaction to the VA's efforts to deal with your objections to the implementation of A-76 in the VA?

AFGE RESPONSE. We have been quite disappointed by the response of VA managers to our efforts to ensure that contracting out does not reduce the level and quality of health care and other veterans benefits. In fact, VA has rejected virtually everyone of these efforts, while at the same time various VA managers claim to be concerned about, or even opposed to, contracting out.

In March 1980, AFGE and VA conducted negotiations on the procedure for implementing contracting out. Further considerations on applying A-76 to VA were deferred until the negotiations on a general collective bargaining agreement between AFGE and the VA.

In October 1980, AFGE proposed an article on the contracting out of bargaining unit work for inclusion in its collective bargaining agreement with the VA. The most important elements of that proposal were:

- (a) requiring notice and detailed information of proposed contracting out.
- (b) requiring that A-76 and the negotiated agreement be complied with prior to implementing contracting out.
- (c) requiring the cost estimate to be based on the same scope of work so that the quality of care was not reduced.
- (d) requiring that statements of work be finished in time so that they can be thoroughly reviewed.

(e) requiring that disputes over accuracy of statements of work be resolved by an impartial third party.

(f) prohibiting use of contracting out to circumvent a personnel ceiling.

(g) requiring that the most efficient and cost effective organization be used in comparing in-house costs.

(h) requiring an assessment of the economic impact on the community and of the effect on the VA missions caused by contracting out.

The concerns reflected in our proposals are precisely the concerns that VA managers have claimed they share when they appear before congressional committees. A prime example is the requirement that a statement of work be accurate and complete, yet they have consistently refused to agree to making this a requirement. VA's prototype statement of work for food services, with its omission of special diets as an integral requirement, is merely one predictable result of VA's failure to agree that work statements must be accurate and complete. After we brought this obvious deficiency to the attention of Congress, VA is now saying that the prototype statements must be accurate and complete. We cannot help but wonder what other inaccurate or incomplete statements of work, not yet subjected to congressional scrutiny, the VA is protecting by this refusal.

AFGE has always sought to work together with VA managers in ensuring the highest quality and most cost effective health care for the veterans of America's armed services. We are disappointed that VA managers have not brought a similar commitment to our negotiations on procedures for implementing contracting out in the Veterans Administration.

Chairman SIMPSON. If you will proceed, Mr. Kearney.

Mr. KEARNEY. Thank you very much, Senator. It is nice to be here this morning with all of these distinguished people.

My summary statement is, as a veteran of two wars and as AFGE's national vice president for New England where I represent VA hospital employees, I am alarmed again at another assault on the facilities that provide a vital service to the men and women who have served their country, and in many cases, sacrificed their physical or mental health in that service.

These facilities must be retained to provide a high level of competence if we, as a nation, are to live up to our commitment to those who have served our country. I might add that hospital services such as dietetic, housekeeping and maintenance are an integral part of the overall effort to provide our veterans quality care.

The contracting out of vital services will destroy the effectiveness of the hospital team when hospital management loses control over the aforementioned services. We, from my office, have surveyed 10 major hospitals in the Boston area, and none of them are contracting out any major services.

Those hospitals are: University Hospital, Children's Hospital, Massachusetts General Hospital, New England Medical Center, Salem Hospital, Faulkner Hospital, Peter Bent Brigham, Beth Israel Hospital, Carney Hospital, and Boston City Hospital.

A major article on contracting out, published by the American Hospital Association indicates that contracting out was not cost effective, that the contractor was not responsible to hospital management when problems occurred, and that contracting out entailed escalating costs in the contract. So it really costs more in the end. In summary, that publication indicated a failure to save money as predicted. Also, the article indicated that the contract company did not live up to the standards expected in the hospital.

If the private hospitals in the United States are experiencing difficulties with contract people, then we should be wary of forcing it or pushing it on the VA.

In looking at a typical large city VA hospital—such as Boston—and the housekeeping, engineering and dietetic functions that are affected by contracting out, we found that over 50 percent of the employees were veterans themselves. At Togus, Maine, in two departments, over 90 percent were veterans themselves, and all of them had at least 15 or 20 years of service.

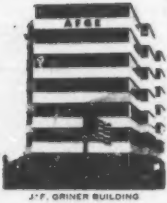
We are also told by management at this hospital that they were quite concerned over losing control of the services of their personnel. We found that a hospital needs a constant and steady work force, while, historically, contractor personnel are mainly part-time help who are moonlighting. In effect, contracting out did not provide the structured and organized control of conditions needed by hospital administration to manage their departments.

The remarks above concerning VA Boston and its departments could be repeated for every Veterans' Administration hospital in New England. It should be noted that the VA hospitals in Togus and White River Junction are physically located in isolated areas and could not call on any qualified contractors locally to perform the work required. The bids would have to come from some larger metropolitan areas.

It is the intent of this Government that it is supposed to be a model employer. How then can it destroy the livelihood of those affected by contracting out to a bidder who, after they are displaced, must give them first offer of employment—oh, yes—but at about \$2 less an hour. Our experience has proven that as soon as these contractor employees are on the job, they will be quickly unionized due to low wages and lack of fringe benefits. They may indeed have to strike in order to get a fair package. But you can bet that the cost which OMB seeks to save will dissipate.

Chairman SIMPSON. Thank you very much.

[The prepared statement of Daniel J. Kearney, national vice president, American Federation of Government Employees, follows:]



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TO DO FOR ALL THAT WHICH NONE CAN DO FOR ONESELF

PREPARED STATEMENT OF

DANIEL J. KEARNEY
FIRST DISTRICT (NEW ENGLAND)
NATIONAL VICE PRESIDENT

AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL-CIO

BEFORE THE

SENATE VETERANS' AFFAIRS COMMITTEE

ON

CONTRACTING-OUT OF VITAL SERVICES IN THE
VETERANS ADMINISTRATION

NOVEMBER 5, 1981

As a veteran of two wars and as a National Vice President for New England where I represent Veterans Administration Hospital employees, I am alarmed again at another assault on the facilities that provide a vital service to the men and women who have served their country, and in many cases, sacrificed their physical or mental health in that service.

These facilities must be retained to provide a high level of competence if we, as a nation, are to live up to our commitment to those who have served our country. I might add that hospital services such as dietetic, housekeeping and maintenance are an integral part of the overall effort to provide our veterans quality care.

The contracting out of vital services will destroy the effectiveness of the hospital team when hospital management loses control over the aforementioned services. We have conducted a survey of all major

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private hospitals in the Boston area. Out of 10 hospitals surveyed none of them are contracting out any of their major services. We found one relatively small hospital (300 beds) in Everett, MA who contract out the dietetic services. As we understand, the food is delivered pre-packaged, heated and then brought to the patient.

In another instance, AFSCME, who represents 15 state and county hospitals in Massachusetts, tells us that none of the hospital functions are contracted out.

Another item that should be of interest to the committee is an article appearing in Hospital Magazine which is the house organ of the American Hospital Association.

It is entitled: "Contract Housekeeping: Hospital Survey Cites Reasons for Termination"

Some of the responses by the hospitals that participated are:

1. "Administrators' comments about the cost-effectiveness of the contract services included: It was not cost effective. The actual cleaning job was one of the key things. It just wasn't being done. And, we felt that by eliminating the contractor we could decrease our costs by cutting out their management fee."
2. "One administrator expressed the lack of accountability this way. The hospital wasn't very clean. We had a lot of trouble and many patients complained. In addition, we didn't receive an effective response from the company when we would notify them of difficulties or problems."
3. "Another respondent mentioned trouble over the contract agreement. We had escalating costs in the contract that began to jump dramatically. We had a construction project going on, and as the contractor began to take over the responsibility of the new square footage, the contract was changed several times. We felt the changes were a little bit more than they were worth."
4. "The main reasons cited by respondents for giving companies lower overall performance ratings were the dissatisfaction of other hospital departments with the contractor housekeeping services and the administrator's feelings that the hospital was losing control over the housekeeping department. Other factors that contributed to low performance ratings were the failure to save money as predicted, dissatisfaction with the assigned director of housekeeping, and the feeling that the personnel who were hired by the contract company did not live up to the standards expected by the hospital."

Let's look at a typical large city Veterans Administration Hospital (Boston) and the functions that are threatened by contracting out. Let's us begin with the Housekeeping Department (Building Maintenance).

There are a total of 97 full-time employees. 19 are Veteran Rehabilitation Act appointments and 36 are veterans. In other words, 55 of those employees are veterans. Also the average years of service for these workers is 23 years. It should be added that approximately 60% of those employees are minorities. During discussion with Management of that department, they were quite concerned over losing control of the services that the dedicated men and women, veterans and non-veterans, with many years of service, were providing to maintaining that hospital with conditions which would provide for the health of the patients. Losing control of necessary labor means that you cannot direct them to do work out of their days sequence without being faced with what is called in the business "an extra". Further, it is almost impossible for a contractor to maintain such a large workforce at the levels the contract calls for. i.e. absenteeism is one of the problems that such contractors face with their every day contracts in various buildings around Boston.

Recently we contacted a man now retired who used to be one of the largest cleaning contractors in the Boston area. We asked him, for instance, if he bid and was accepted, how long did it take him to train a workforce to perform the housekeeping functions in a hospital and he estimated that it would be at least 90 days before new employees might be adequate. He further stated that most of the jobs that he was familiar with were performed by part-time help who were moonlighting. A hospital needs a constant and steady workforce. He concluded by stating that in a strike situation, he would be absolutely helpless and the needed services would not be performed.

Engineering Department

The Engineering Department has 80 full-time employees. There are 8 Veteran Rehabilitation Act appointments and 38 veterans with an average service of 12 years. The Engineering Department has a dual responsibility for the upkeep and maintenance of millions of dollars worth of equipment. The department must be ready at any given moment to make emergency fixes, no matter how extensive the work may be. Another very important function is to have an on-going preventive maintenance program and unless you have dedicated mechanics and close supervision, proper preventive maintenance will not be done. A contractor, in the interest of increasing his profit, could neglect preventive maintenance and the customer would not become aware of that neglect until the hospital suffered a whole series of breakdowns of systems and equipment.

President Hunt and I questioned Management in that department and asked them how many different contracts would they think they would have to let in order to perform all of the services needed in that department. The response was illuminating, as we were told that it might have to be as many as seven (7) different contracts; meaning that hospital management would almost be helpless in trying to coordinate the various trade groups. Again,

of course, the hospital would be faced with strikes in that department and that right after the onset of such an incident, the whole hospital would cease to function. This kind of an incident would cost our veteran patients very very dearly.

Dietetics Department

There are 99 full-time employees with 24 part-time employees. Of the full-time employees, four (4) are Veteran Rehabilitation Act appointments and 34 are veterans. The average service for that department is 18 years. The dietetic department bears a heavy responsibility for providing service to the patient. Their job begins with the purchase of food and the inspection of such food to see that it lives up to specifications. Then they are responsible for the preparation of wholesome, pure food. Nothing must be left to chance in that kitchen. Every measure must be taken to see that antiseptic conditions are maintained at all times up until the delivery to the patient. The kitchen is responsible for providing up to 24 different diets. Those employees are under careful scrutiny by the clinical dietitians. If that function was offered for bid, many doubt that there are any firms in the whole New England area with that kind of experience to bid for that job. More than likely, some firms will, and they certainly might, under-bid the dietetic cost. But from our surveys in this area, they will be woefully lacking in experience to do such a comprehensive job.

It should be noted here, for instance, that the contractor will be assuming responsibility for nearly three million dollars worth of equipment needed to run that department. He will have a responsibility of purchasing the food for the veterans and he is supposed to live up to Government specifications. Maybe he cannot or won't, in order to make profit. A contractor, whose motivation is profit, would be tempted to cut corners in dietetics requirements and Government specifications. It is awesome to speculate what an ordinary caterer might do with a job that requires so many special diets.

The remarks above concerning Veterans Administration Hospital, Boston, MA and its departments could be repeated for every Veterans Administration Hospital in New England. It should be noted that the Veterans Administration Hospitals in Togus, ME and White River Jct., VT, are physically located in isolated rural areas and could not call on any qualified contractors locally to perform the work required. The bids would have to come from some larger metropolitan areas.

Veterans Administration Hospital, West Haven, CT most closely compares to Veterans Administration Hospital, Boston because they both are in fairly large metropolitan areas.

I would like to conclude by telling you that the threats of contracting out over the past two years is devastating the morale of the employees in those departments who can see their careers crumbling. They are deserving employees; over 60% are veterans themselves.

The people in those jobs, particularly the dietetic and housekeeping departments, are low paid and most of them stay with the job because they care about the veterans they are servicing.

Is it the intent of this Government, that is supposed to be a model employer, to destroy the livelihood of those affected by contracting out to a bidder who, after they are displaced, must give them first offer of employment with \$1.50 per hour cut in pay and no fringe benefits. Our experience has proven that as soon as these contractor employees are on the job, they will be quickly unionized due to the low wages and lack of fringe benefits. They may indeed have to strike in order to get a fair package. But, you can bet that the cost which OMB seeks to save will dissipate. But worse, the kindness and care that the veteran has always been given, will be gone.

I ask all of you here today to reflect on what has been said. Do not let the search for savings turn you all to approving those programs when serious reflection will indicate that history has proven that there will not be savings, just suffering.

See Addendum

ADDENDUM

The American Federation of Government Employees, AFL-CIO is indebted to the following Veterans Administration Hospital Local Presidents who have worked so long to represent Veterans Administration Hospital employees in New England and have provided some statistical data included in this statement. They are:

Dorothy Dedmond - President, Local 1674, West Haven, CT
 Nelson Hunt - President, Local 2143, Boston, MA
 Patricia Warren - President, Local 2604, White Rvr. Jct., VT
 William Rollins - President, Local 2610, Togus, ME

West Haven, CT

- Dietetic Service
87 Full-time Employees - 41 Veterans
- Building Management Services
76 Full-time Employees - 34 Veterans
- Engineering Services
69 Full-time Employees - 54 Veterans

White Rvr. Jct., VT

- Dietetic Service
36 Full-time Employees - 15 Veterans
- Building Management Services
35 Full-time Employees - 27 Veterans
- Engineering Services
51 Full-time Employees - 41 Veterans

Togus, ME

- Dietetic Service
95 Full-time Employees - 55 Veterans
- Building Management Services
85 Full-time Employees - All Veterans
- Engineering Services
94 Full-time Employees - All Veterans

Chairman SIMPSON. Just a question, and then I must turn over the hearing to Senator DeConcini who is very graciously assisting me as I go to a different appointment.

Do you have any statistics on the levels of compensation that were paid to displaced Federal employees who were subsequently rehired by the contractor as compared to the compensation that the worker would have received if he had remained in the Federal employment?

Mr. KEARNEY. The prevailing rate, for instance, in the Portland-Augusta area where the Togus VA Hospital is, is \$4.25 an hour. The contractor was supposed to pay that. The wages of those employees at the hospital in Togus are about \$5.50 an hour. So, in that case, they would lose considerable, \$1.25 an hour.

Mr. BLAYLOCK. Mr. Chairman, in general that is a mixed bag though. We have examples, and we don't obviously have that many examples of contracting out in VA at this point in time as we are just moving into that, but DOD contracts now have been in for quite some time. We have examples of contractors, for instance, around the Cape Kennedy area, the contractor's salary rates much exceed the rate of the Federal Government, and also the fringe benefit package. As yet it continues to go contract. In other cases contractors primarily use what we term a flesh-peddling operation. They bring in a body only at lowest wage possible with no fringe benefits. So it is a mixed bag at this point across the country.

Chairman SIMPSON. The thing is, I want to be sure the record reflects that the VA is no stranger to contracting out. The VA has been involved in contract services since 1955, and this year services are \$700 million. So it is not some new approach. I think we want to keep that in mind.

If you could furnish us any statistics which you have, we would be very appreciative. And I would ask then, do you have any statistics to show how many of the displaced employees who were rehired by the contractor remained on the job for any significant period of time, and how many may have left soon after they were rehired. That would be of interest to the committee.

Mr. BLAYLOCK. We will see if we can get some of that information to you.

Chairman SIMPSON. I would appreciate that.

Mr. BLAYLOCK. And also their compensation level if it is possible to make some comparisons with.

Chairman SIMPSON. Yes. That would be very helpful. I thank you very much. I am going to turn over the hearing to Senator DeConcini, and I appreciate his good service. He has been a very active member of the committee.

Thank you, Mr. Blaylock and Mr. Kearney.

Mr. BLAYLOCK. Thank you, Mr. Chairman.

Chairman SIMPSON. Let me ask one other question if I might, and then Senator DeConcini may have one. That DOD experience indicates apparently that approximately 90 percent of the employees displaced by the contracting out process were rehired by the contractor. That is the figure we have. Could you comment on the significance of that figure as it relates to your concern about the dilution of veterans preference rights?

Mr. BLAYLOCK. I am not in a position to validate that 90 percent figure, but you know one of the provisions put into OMB Circular A-76 was that there would be a right of first refusal to any employees who were displaced by the contract. It requires the contractor to give them the right of first refusal. As to the validity of that percentage factor, I am not in a position to verify that at this point.

Chairman SIMPSON. Thank you very much.

Senator DECONCINI [presiding]. Mr. Kearney, Senator Mitchell could not be here at this time, and he sends his regrets, and he asked me to ask a couple of questions. So for the record, could you respond to Senator Mitchell's questions.

Are you aware of any hospitals that have had problems with employee strikes?

Mr. KEARNEY. Yes. Two in Massachusetts about the same time, and I will give you one example. At the Cape Cod Hospital, which is a private sector hospital at Sandwich on the Cape, the nurses went on strike. They had to close the hospital and there were 300 patients transferred, some as far as Boston.

Now, Senator, if that happened at Togus VA where there are 700 or 800 veteran patients, there would almost be, wouldn't be any place to put them. You might have to helicopter them to Boston, for instance, in order to find beds for them. So it is a horrendous situation to contemplate.

Senator DECONCINI. Well, you also answered a second question. He asked about the effect of a strike in the dietetic or maintenance service in the Togus VA facility in Maine.

Mr. KEARNEY. Senator, they said that if housekeeping struck you could put up with it a couple of days. If dietetic services struck, you only have 3 hours of grace period between a meal. You have to perform.

Senator DECONCINI. Thank you very much.

Mr. Blaylock, on page 11 of your statement you recommend as a check of escalating contract prices an absolute requirement that an agency retain a core inhouse capability. Could you explain how this requirement would work in the case of, for example, a VA hospital contracting out their laundry and custodial services?

Mr. BLAYLOCK. Well, the basis for that contention is that Government has a constitutional and statutory responsibility to provide certain services. In this case it is treatment of veterans. If the agency loses that core capability of maintaining that service in a situation such as Dan and you just talked about that goes private sector and a strike occurs, in this case, how would that hospital provide meals to those patients within a 3-hour timeframe. If you have lost that capability, you are then at the mercy of that contractor. Because you no longer have the personnel to do the job, you may no longer even have the equipment or facilities to do the job. So then you have removed one of the elements that is supposed to bring about more efficient operation, that element is competition. You are not in a position to compete with them.

Senator DECONCINI. I take it you say it is not feasible to maintain an inhouse core capability.

Mr. BLAYLOCK. We think it is. Of course, if you connect that with our total statement, we think in this case that treatment of veter-

an patients is an inherent government responsibility that should not be contracted out.

Senator DECONCINI. Well, let's say we do contract out for purposes of discussion.

Mr. BLAYLOCK. For what purpose?

Senator DECONCINI. Just for discussion.

Mr. BLAYLOCK. I was seeing if you had a good reason. OK, we will talk about it.

Senator DECONCINI. Like Senator Simpson said, we already contract out some \$700 million. So it is a fact of life. But for purposes of discussion, if you do contract out one of the services, in your judgment should there be an inhouse core capability?

Mr. BLAYLOCK. If you contract it out you have lost that core capability. How can you contract it out and maintain it? No.

Senator DECONCINI. That is the point. Should you try to keep a skeleton core capability?

Mr. BLAYLOCK. You know, you may have your managers there, and say you have a supervisor and two meat persons in the kitchen. They are obviously going to do the best they can to feed the 700 patients. But you have lost your core capability if you contract. It is one of the points that we make.

Now there are certain functions in other agencies of Government where because of the ability to transfer rapidly and whatever you still have a core capability, you still have the facility, equipment or what have you. This is a function we don't think you can maintain that capability in certain areas and contract it out.

Senator DECONCINI. You make a good point. My last question, can you expand on the effects on the VA employees' morale as a result of implementation of A-76?

Mr. BLAYLOCK. Well, I can do that specific and in maybe somewhat general terms. We represent, as you well know, about 700,000 Federal workers, about 110,000 of those are VA people. I would say that there are two groups of workers we represent who are extremely loyal to the mission of their agencies and the recipients of the services they provide. That is our employees in the Veterans' Administration and our employees in the Social Security Administration. They are very sensitive to the needs of those patients that they treat and care for. And that is their priority.

The Veterans' Administration over the years has provided good hospital care and treatment for veterans. The employees can't understand why at this point in time the employer, the Government, would be even thinking about putting their job on contract. They have demonstrated that they do a good job for these patients. To them patient treatment is the prime issue. They just don't understand it. So it is having a devastating effect on the morale of employees, no doubt about it.

As a specific example, I had a group of doctors in Virginia who were totally up in arms at a VA hospital. VA had contracted out the secretarial service there. So as they toured the wards and did their examinations on patients, the doctors made their notes. And then those notes were shipped from that hospital up here to Washington, D.C. for typing. With about a 10- or 11-day turnaround period, they couldn't even go back and get a patient's file to review

what had happened the day before. They couldn't understand. It didn't make any sense from a purely practical point of view.

Senator DECONCINI. So not only in that case did the morale slip, but also the efficiency of delivering any kind of a service.

Mr. BLAYLOCK. Very definitely. You are a doctor that comes on the shift today and you try to find a patient's charts and records from the doctor that examined him on the previous shift, and they are on a bus to Washington, D.C. What do you do? Start all over?

Senator DECONCINI. Very good. Do you have any questions to submit? We do have questions and we will ask you to submit them to us for the record. Senator Cranston also has some.

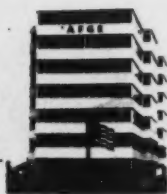
Yes, sir, Mr. Kearney?

Mr. KEARNEY. Just one statement. That story from the Air Force people about some contracting out they had at the Hill Air Force Base, I believe it was about 50 jobs they contracted out, it is a base with 15,000 there. It is easy to place those people. But you can't place people in White River Junction, Vt., or in Togus, Maine, et cetera. It is just impossible to place that many people in local industry, and there are no Government installations to absorb that kind of labor. It was easy for the Air Force to do these things.

Senator DECONCINI. Very good. Thank you.

Thank you for your testimony. We appreciate hearing from you today.

[The following prepared statements and letters were submitted for the hearing record by Kenneth T. Blaylock and Daniel J. Kearney of the American Federation of Government Employees:]



J. F. GRINGER BUILDING

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TO DO FOR ALL THAT WHICH NONE CAN DO FOR ONESELF

PREPARED STATEMENT FOR THE RECORD OF

VIRGINIA O'DELL
PRESIDENT, AFGE LOCAL 2547
VA MEDICAL CENTER IOWA CITY, IOWA

ON

VA CONTRACTING OUT IN IOWA CITY

NOVEMBER 5, 1981

My name is Virginia O'Dell and I'm president of AFGE Local 2547 at the VA Medical Center in Iowa City, Iowa. I've been a nurse for 17 years, the last six of them in the VA. I work in "hospital based home care," which is one of the special health care programs of the VA. By treating patients in their homes, we eliminate unnecessary trips to the clinics and shorten hospital stays. This helps VA save money which it then uses on other medical care.

Most of the VA employees in Iowa City are veterans, and they include disabled veterans and several former POW's. They are proud of their jobs in the "veterans caring for veterans" program.

The single most important message I want to give this Committee is that we don't have to wait for contracting out to hurt the VA. A-76 and contracting out has already harmed the VA hospital system. I cannot tell you how often I'm asked by other VA employees whether they'll still have a job. "Virginia," they ask, "should I sell my

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home because I won't be able to meet the payments if my job is contracted out." Others have saved money and are thinking of buying a house. They ask if they should buy.

Frankly, it angers us out in the field because we know how important our work is. We have the feeling that someone in OMB decided we were going to be contracted out, regardless of what it cost either in money to the VA or in care to the veteran.

Many of the VA patients have read about OMB's plan for contracting out in VA hospitals in their veterans service publications. The patients waver from being fearful to being furious.

I'm proud to say that I work in a VA hospital. From the first day on the job, VA employees learn that our job is to serve the veteran. Our rule is the patient comes first. And since many of the employees are also veterans, they know that they may be in the hospital one day. So they take extra care to see that they do indeed serve the veteran.

Frankly, its not the same with the contract employees we already have working in Iowa City.

We contracted out maintenance of our boiler plant and our chiller plant. Last spring the chiller plant just couldn't seem to get the air conditioning in the operating rooms right, and I was told that the contractor had put in the wrong refrigeration pipes and our in-house workers had to fix it. In 1979, the contractor's employees for the boiler plant caused a fire by welding in an area filled with coal dust. The fire spread through the mail shutes, and the fire trucks couldn't get to the fire because the contractor's vehicles blocked the fire lanes. Ten VA employees wound up in the medical intensive

care unit with severe smoke inhalation because they fought the fire.

As a nurse, I want to stress how important to patient care are the activities of a lot of workers whose jobs are targeted for contracting out. We had contract carpenters who worked in a surgery ward but didn't bother to put up dust barriers. You could see clouds of plaster dust in the air as you walked down the hall. They carted off the old plaster in open wheelbarrows, and patients, nurses, visitors, and volunteers had to walk through their spillage. Patients on that ward all had new surgery wounds, and many developed staph infections because of the dirt. In fact, surgery was suspended in the ward for a while. I'm not saying the contractor's employees did this on purpose. They were hired, by the contractor, to tear out a wall. But where was their concern for the VA patient? VA employees rarely are so shortsighted. The veteran comes first.

Our janitors are an important part of the health care team. When the janitors attend to all their duties--cleaning the rooms and furnishings, wiping up unexpected spills, and others--the nurse is available to provide patient care. If a contractor tries to make money by relying on a transient, minimum wage work force--I can guarantee the nurse will end up swinging mops instead of nursing patients.

As a nurse I also know the groundskeepers contribute directly to patient care. At Iowa City, we have 3 groundskeepers and about 20 patients who help them either in a voluntary or minimum wage capacity. Their work outside, whether planting flowers or trimming hedges, has a therapeutic value for these patients that you couldn't possibly measure in an OMB circular. Because the groundskeepers are veterans,

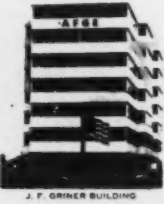
they make sure that the patients' work is as beneficial as possible. Can an outside contractor--whose goal is a higher profit--be relied on to do the same? Of course not. As a nurse though, I want you to know that you can see the difference in these patients when they are able to put in their work on the grounds.

Finally, I want to leave this Committee with two thoughts. As a nurse, I wonder who will be in the kitchen fixing the special diets or in the laundry cleaning the linen when the contract employees go on strike? Our contract employees in Iowa City have already engaged in strikes. Fortunately, we had enough VA employees who cared enough to spend extra hours getting the contractors' job done.

VA employees have never gone on strike--not even when we didn't get our paychecks last year because the appropriations bill hadn't passed.

My last thought is really a special plea. Congress has to do something so that VA employees--all Federal employees really--stop falling further behind everyone else in pay. We got a 4.8% increase this year. Right across the street, the University of Iowa hospital employees got 8%. I don't believe their standard of care exceeds ours. For comparison, the municipal fire department got a 14.2% increase.

VA employees deserve a fair wage, just like everyone else. They do not deserve the stress and turmoil of wondering whether they're going to lose their jobs because someone behind a desk at OMB in Washington--who I would bet isn't even a veteran--decided that VA hospitals no longer need VA employees. We wonder if OMB's next decision will be that veterans no longer need VA hospitals.



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TO DO FOR ALL THAT WHICH NONE CAN DO FOR ONESELF

PREPARED STATEMENT FOR THE RECORD OF

ARTE I. PIERCE
PRESIDENT, NATIONAL COUNCIL OF VA LOCALS
AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES

BEFORE

COMMITTEE ON VETERANS' AFFAIRS
UNITED STATES SENATE

ON

CONTRACTING OUT IN THE VETERANS ADMINISTRATION

NOVEMBER 5, 1981

Mr. Chairman, members of the Committee. My name is Arte Pierce, and I am President of AFGE's National Council of VA Locals. We are the representative for some 110,000 employees in the Veterans Administration. I've been a VA employee for 32 years. I started in 1949 as a messenger, rated CPC-2 or otherwise known as "lower than GS-1." Becoming a file clerk was a promotion. Later, I was appointed file clerk supervisor--so I have spent time on the management side of the table, too. Eventually, I became an educational benefits specialist and then a claims examiner or adjudicator. After working as senior adjudicator, I became a GS-12 disability rating specialist which is the work I now do.

HELP SAVE OUR BENEFITS

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In these jobs I have dealt with veterans and the veterans service organizations on a daily basis. I can report that veterans share our concern at the adverse effects on contracting out of their medical and other benefits. As a long-time VA employee, I would like to make a few remarks on contracting out from the operational perspective.

The primary objective for the Veterans Administration and its employees is to render service to the veterans of the armed services. Neither the VA nor any of its employees benefit by skimping on service. The primary objective for any outside contractor, however, is to cut operating expenses in order to secure greater profits. We don't believe that care for veterans should be subjected to the pressure caused by a desire to boost profits.

The VA's own contracting out experience already demonstrates how scarce moneys can be taken from medical care. Medical laboratory tests have been contracted out by various medical centers. In Cincinnati, for example, the projected costs for contracting out laboratory tests was \$160,000 for FY 1979. The Inspector General found that, even if the contractor's fees were lowered, the in-house cost would be \$81,000 and ordered laboratory testing returned to in-house performance.

The intrusion of "profits" into the health care system will likely have other adverse effects besides the siphoning off of scarce funds. Since quality control is so loose in contracting out, contractors will have an interest in keeping their employees on minimum wages when possible. This would result in the VA contracts becoming an employer of transients who stay with the contractor only

until finding better employment. This would cause constant turnover and disrupt stability of vital VA operations.

I would hope that medical center directors and the service chiefs would have control over the contractor, but it is obvious that they would have no control over the contractor's employees. In fact, paragraph 6(d)(2) of A-76 specifically provides that the Circular "will not be used as authority to enter into contracts which establish a situation tantamount to an employer-employee relationship between the Government and individual contract personnel."

For VA patients, this removal of control over the workforce from the actual operating personnel can be quite serious. Hospitalized veterans on numerous occasions find it necessary to have their diets changed from one meal to the next. This can be readily accomplished at present with simple instructions from the attending physician to the dietician. A private contractor, however, is unlikely to have such a quick response time. Similarly, response time is critical in the event of any breakdown in hospital equipment during surgery or the need to institute immediate infectious control measures. We presently have in-house personnel who can meet these needs, but once contracting-out is underway, it is probable that the contractor will be unavailable for at least some of these "routine emergencies."

Much of the VA's experience with contracting out is with skilled trades--painter, electricians, plumbers and others. Often, the in-house personnel have to complete or do correctly the job which the VA contracted out. In 1979, the contract painters called in to the VAMC Denver, Colorado, partially completed the job and then left. It was necessary to use our own in-house painters to do the job.

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In this case, the VA had made an advance payment to the contractor for work that they never completed. Similar problems occurred with the contracting out of other skilled trades at the Medical Centers in North Chicago, Marion, Illinois, Allen Park in Detroit, Ann Arbor, Michigan, Poplar Bluff, Missouri, and Danville, Illinois. It is hard to see how this experience justifies expanding the number of functions being contracted out.

I'm proud to say that I'm a veteran of World War II. I served in the U.S. Army for 35 months, 23 of them in the European theatre. Many VA employees are veterans. Whether in the regional office or on the hospital floor, we're proud to be a part of the "veterans caring for veterans" program. Medical center directors themselves fear the outside contractors will not display the same concern and sensitivity to veterans' needs as VA employees now routinely provide. As veterans ourselves, we share that fear. All we are asking is to be given the chance to continue doing the job. We appreciate the Committee's continuing concern and support for the Veterans Administration and we promise you our cooperation.

American Federation of Government Employees

AFFILIATED WITH THE AFL-CIO

LOCAL NO. 2143



VETERANS ADMINISTRATION HOSPITAL

JAMAICA PLAIN, MASS. 02130

November 10, 1981

Mr. Daniel J. Kearney
National Vice President
AFGE District 1
295 Turnpike St
Canton, Ma. 02021

Dear Dan:

1. This letter is in regards to the testimony presented by you and AFGE National President Ken Blaylock, to the U.S. Senate Veterans Affairs Committee, in Washington, D. C., November 5, 1981, on "Contracting Out Of Vital Services in the Veterans Administration".

2. Unfortunately, due to the time limitation for presenting testimony before the Committee, we Local Presidents who were present were not able to address the Committee personally, however, for the record, the possibility that vital V. A. Services, may be contracted out, has had a very negative effect on the morale of the patients and employees at this Medical Center.

3. If vital services are contracted out in the V. A., it will greatly compromise the ability of the V. A. to continue to give quality care to our veterans. This fact came to light when I questioned local V. A. local V. A. managers, who stated that, "when services are contracted out, local managers have no control over the contractor's employees, or the way work is done or assigned to the contractor's employees". Whereas, vital services performed by V. A. employees, the local managers have complete control over the quality of services rendered, and are in the position to control costs for these services.

4. V. A. employees are loyal and compassionate workers, and can be relied on in any emergency to do their part, no contractor can give this assurance, America's War Veterans Deserve The Best Medical Care And Assistance This Country Can Give, The Veterans Administration was given this Mandate by the Congress of these United States, I sincerely hope that the current administration does not compromise this mandate, by Contracting Out Vital V. A. Services, on the premise that it is cost effective to do so.

Fraternally Yours,

Nelson Hunt, President
AFGE Local 2143



AFL-CIO

American Federation of Government Employees

LOCAL LODGE 2604

WHITE RIVER JUNCTION, VERMONT 05001

NOV 17 1981

November 10, 1981

Dan Kearney, NVP
AFGE District #1 Office
295 Turnpike St.
Canton, MA 02021

Dear Dan:

Relative to the question regarding morale at our Station, it can all be said in a very few words. It has been and still is terrible for over 2 years now since A-76 came up to the surface here at our Station. The worse the morale gets the more productivity goes down and patient care can only be affected adversely. Employees are constantly reminded by Management of the possibility of their job being "contracted out" and yet expect all employees to be increasing productivity. In fear of losing their jobs several employees have transferred to lower paying positions in ones they feel are more secure than theirs, especially the DVB employees.

I have found also that the sick leave has increased with employees in Divisions where there is a shortage of staff and refusal of Management to fill these positions to keep costs down.

Again, I cannot express how bad morale is here in WRJ, VT and all due to the constant threat of A-76. It seems some final decision on this must be settled soon with Congress.

I would like to take this opportunity to thank you again for the chance to appear before the Senate Veterans Affairs Committee and all the courtesies you extended to me.

Thank you.

PATRICIA WARREN
President

Senator DECONCINI. Our next witnesses will be Mr. William Pollard, president and chief operating officer, ServiceMaster Industries, Downs Grove, Ill., and Mr. George Daoust, executive director, National Council of Technical Service Industries, Washington, D.C.

Mr. POLLARD. Thank you, Mr. Senator, for the opportunity to appear before you today.

Senator DECONCINI. Please proceed.

Mr. POLLARD. Of course, I have a written summary that I have submitted to the committee, which I would like to have introduced into the record, and I will have a brief overview as far as an oral statement.

To my left is Roger Ervin from ServiceMaster, who is working in our Government relations with respect to the contracts we have.

Senator DECONCINI. Excuse me, Mr. Pollard. We are also joined here by Mr. Netterstrom, president-elect of Building Services Contractors Association—excuse me, for missing you.

And we have one other person with you today.

Mr. DAOUST. George Daoust.

Senator DECONCINI. You're George Daoust—and the other person?

Mr. POLLARD. This is Roger Ervin from ServiceMaster Industries.

Senator DECONCINI. Very good. Thank you.

TESTIMONY OF A PANEL CONSISTING OF C. WILLIAM POLLARD, PRESIDENT AND CHIEF OPERATING OFFICER OF SERVICEMASTER INDUSTRIES, INC., ACCOMPANIED BY ROGER N. ERVIN, DIRECTOR OF FISCAL MANAGEMENT; DR. GEORGE A. DAOUST, JR., EXECUTIVE DIRECTOR, NATIONAL COUNCIL OF TECHNICAL SERVICE INDUSTRIES; AND JAMES S. NETTERSTROM, CBSE, PRESIDENT, SHIP SHAPE MAINTENANCE CO., INC., AND PRESIDENT-ELECT OF BUILDING SERVICE CONTRACTORS ASSOCIATION INTERNATIONAL

Mr. POLLARD. I'm president and chief operating officer of ServiceMaster Industries, and as we come before you today, we are speaking, of course, on the issue of A-76 and section 601.

We believe that the issue before you today goes far beyond section 601. It raises a basic question of Federal policy, namely, is the Federal Government, through its various agencies of health care and other related services, willing to practice what it has preached and mandated to the private health-care sector, to contain and reduce health-care costs through increased utilization and improved productivity?

One way that the private sector is responding to this challenge is the use of supportive management services provided by firms such as ServiceMaster.

We submit that not only the VA, but every agency of the Federal Government should be encouraged—in fact, directed—to open up and consider these proven management services as a way of using the competitive forces of the free enterprise system to assist in bringing improved quality of service with increased productivity.

ServiceMaster is the leading provider of management services to the health-care community for the nonmedical support departments of housekeeping, plant operations and maintenance, laundry

and linen services, clinical equipment maintenance, materials management, and food service management.

We currently provide our services in over 950 health-care facilities, which include hospitals ranging in size from fewer than 50 beds to over 1,000 beds.

We serve all major segments of the health-care community, including large university and teaching facilities; multiple hospital systems, both proprietary and not-for-profit; Hospitals owned and operated by local and State governments; and local community hospitals.

With the exception of U.S. Air Force hospitals, the only significant segment of the health-care community not open to these management services is hospitals operated by agencies of the Federal Government.

Our service is a management service, which is typically provided by our onsite manager managing the hospital's employees to perform the designated function in accordance with agreed-upon standards, at a guaranteed overall cost.

It is important to note here that as an alternative to having all of the employees on the contractor's payroll, our service can be delivered to VA hospitals using, not replacing, their existing labor force, including those in the labor force who are veterans.

What are the results of our efforts in the health-care community?

We have initiated an energy management program, for example, which was cited at the national convention of the American Hospital Association. We were commended for reducing energy consumption an average of 18 percent, over \$5.7 million in the hospitals we served, a reduction of 770 billion BTU's, enough energy to power 31 100-bed hospitals for 1 year.

In the past 4 years we have introduced seven major technical improvements in our housekeeping programs.

The chemicals and cleaning products and equipment that we use in the delivery of our management system are developed and manufactured by us. However, we are not in the business of simply selling products. Our business is based upon the delivery of an efficient management program.

Unlike some product peddlers who have testified on this issue and have worked on high profit margins for the desire to simply increase the product usage, ServiceMaster is interested in reducing the overall product usage.

For example, in one recent equipment innovation we succeeded in reducing by two-thirds the amount of germicidal disinfectant required for cleaning hard surface floors, while reducing the bacteria count and shortening the labor time as well.

Why shouldn't the Federal sector be open to the dynamics of these benefits?

As I mentioned earlier, the only Federal segment using hospital supportive management services is the U.S. Air Force.

We have had the privilege of serving in a number of these hospitals, and in addition to improving overall costs we have been able to significantly reduce employee turnover, add job skill training and education, and provide, for example, in one such facility an op-

portunity for over 30 housekeeping employees to earn their high school degrees.

Congressman Dan Rostenkowski, chairman of the House Ways and Means Committee and former chairman of the Subcommittee on Health, noted in an address given a few years ago the significant contribution that ServiceMaster has made to the health-care community. He commended ServiceMaster for its efforts in delivering a more organized and efficient supporting management program.

At that time he encouraged us to continue to participate in the process of increasing the efficiency of health care. We believe that our appearance here today is in furtherance of that word of encouragement.

As president of ServiceMaster and as a member of the board of the National Committee on Quality Health Care, I am interested in seeing that the Federal sector has available to it the same programs and benefits that have been proven in the private sector.

It is not necessary to spend \$10 or \$20 billion to make this analysis. We suggest that the VA undertake a pilot program involving a responsible and responsive management firm serving a select group of VA hospitals, to determine the benefits of supporting management services.

The results of this pilot program could then be shared with this committee and further consideration could be given as to whether the program should have systemwide application.

The time and cost for considering such a pilot program would be nominal.

Thank you.

Senator DECONCINI. Thank you very much, Mr. Pollard.

[The prepared statement of C. William Pollard, president and chief operating officer of ServiceMaster Industries Inc.; and ServiceMaster Industries' responses to written questions submitted by Hon. Alan K. Simpson, chairman of the Senate Committee on Veterans' Affairs, and Hon. Alan Cranston, ranking minority member of the Senate Committee on Veterans' Affairs, follow:]

PREPARED STATEMENT OF C. WILLIAM POLLARD, PRESIDENT AND CHIEF OPERATING
OFFICER OF SERVICEMASTER INDUSTRIES INC.

Mr. Chairman and distinguished members of this Committee, I am C. William Pollard, President and Chief Operating Officer of ServiceMaster Industries Inc. Thank you for the opportunity to appear before you today and testify concerning the effects of Circular A-76 of the Office of Management and Budget on the Veterans Administration. Through the attachment of a rider to the recently signed Public Law 9766, the Veterans Disability Compensation and Pension Amendment of 1981, the VA has effectively been restricted from implementing the intent of Circular A-76. This rider, Section 601, limits the VA in its consideration of proven alternatives in the management of supporting departments of a hospital, such as housekeeping, plant operations and maintenance, and food service.

The issue before you today goes far beyond Section 601. It raises a basic question of Federal policy. Namely, is the Federal Government, through its various agencies of health care and other related services, willing to practice what it has preached and mandated to the private health care sector, to contain and reduce health care costs through increased utilization and improved productivity?

One way that the private sector is responding to this

challenge is the use of supportive management services provided by firms such as ServiceMaster. We submit that not only the VA, but every agency of the Federal Government should be encouraged -- in fact, directed -- to "open up" and consider these proven management services as a way of using the competitive forces of the free enterprise system to assist in bringing improved quality of service with increased productivity.

ServiceMaster is the leading provider of management services to the health care community for the non-medical support departments of housekeeping, plant operations and maintenance, laundry and linen services, clinical equipment maintenance, materials management, and food service management. We currently provide our services in over 950 health care facilities, which include hospitals ranging in size from fewer than 50 beds to over 1,000 beds.

We serve all major segments of the health care community, including large university and teaching facilities; multiple hospital systems, both proprietary and not-for-profit; hospitals owned and operated by local and state governments; and local community hospitals. With the exception of United States Air Force hospitals, the only significant segment of the health care community not open to these management services is hospitals operated by agencies of the Federal Government.

The expansion of our services to over 950 health care

facilities, at a growth rate that has required our company to double in size every three years for the past 12 years, is a factor in the marketplace that cannot be ignored. This expansion is documented in the recent article in Modern Healthcare magazine (attached as Exhibit 1) reporting upon the growth in the number of hospitals using some sort of management or contract services.

Our service is a management service which typically is provided by our on-site manager managing the hospital's employees to perform the designated function in accordance with agreed-upon standards, at a guaranteed overall cost. We do not replace administration. We support administration, typically using the hospital's own employees and providing management, motivation, and training of those employees for an improved level of performance. It is important to note here that our service can be delivered to VA hospitals using -- not replacing -- their existing labor force, including those in the labor force who are disabled veterans. This labor force could remain on the Government payroll or it could be directly employed by ServiceMaster, depending upon the needs and requirements of the VA or any of its individual hospitals.

The benefits of our management system for hospitals include:

- * improved quality and consistent delivery of service;
- * cost containment and control;
- * education and training for people development resulting in a motivated work force;

- * improved administrative controls on support service functions through establishment of regular appraisal and review.

Cost containment is a major concern for every health care facility. ServiceMaster has consistently been able to provide management programs with improved quality at the same or reduced cost. And initial cost savings is only the beginning of our effort to help the hospital contain costs. We are constantly developing improvements in our service delivery system which provide additional savings. ServiceMaster has committed substantial resources to the applied research and development of products, equipment, and system improvements. We have the economies of scale to do the development work that no single institution and no other provider can accomplish. What are the results of these efforts? Here are just a few examples:

- * We have initiated an energy management program which has resulted in substantial savings for customers of our plant operations and maintenance program. This program was cited at the national convention of the American Hospital Association. At the opening session attended by 7,000 health care professionals, ServiceMaster was commended for an energy program that reduced energy consumption by an average of 18%, a total of \$5.7 million saved in energy costs. That is a reduction of 770 billion BTUs -- enough energy to power 31 one hundred-bed hospitals for a year.

- * In the past four years we have introduced seven major technical improvements in our housekeeping program. The net effect of these improvements is a substantial productivity increase for hospitals we serve.

- * The chemicals, cleaning products, and equipment we use in the delivery of our housekeeping management system are developed and manufactured by us. However, we are not in the business of selling products. Our business is based upon the delivery of an efficient management program. The products and equipment are used only as a tool in accomplishing an overall result. In housekeeping, for example, products and equipment represent less than 5% of total costs. Although this is a small percentage of the total, it is still important to improve our efficiency in this area. In one recent equipment innovation we succeeded in reducing by two-thirds the amount of germicidal disinfectant required for cleaning hard surface floors -- while reducing bacteria count and shortening labor time as well.

In a competitive environment we have a powerful incentive to continue to improve the benefits of our programs. Unless we establish a differential initially, there is no reason for the hospital to buy our service. Unless we go on to establish a

differential on a continuing basis, there is no reason for that hospital to continue our service. Thus, in order to establish and to continue our business, we must constantly improve. We are a service company, and we cannot rely upon patents, bricks and mortar, or the security of tradition to survive and grow. We must rely instead on customer satisfaction.

Why should not the Federal sector be open to the dynamics of these benefits? As I mentioned in my introductory remarks, the only Federal segment using hospital supportive management services is the United States Air Force system. We have had the privilege of serving in a number of these hospitals, and in addition to improving overall costs we have been able to significantly reduce employee turnover, add job skill training and education, and provide, for example, in one such facility an opportunity for over 30 housekeeping employees to earn their high school degrees. We are in a people business, and people are important and need expanded opportunities for training and education regardless of who they work for, private industry or the Federal Government.

Congressman Dan Rostenkowski, Chairman of the House Ways and Means Committee and former Chairman of the Subcommittee on Health, noted in an address given a few years ago (Exhibit 2) the significant contribution ServiceMaster has made to the health care community, and he commended ServiceMaster for its efforts

in delivering a more organized and efficient supporting management program for hospitals. At that time he encouraged us to continue to participate in the process of increasing the efficiency of the health care delivery system. We believe that our appearance before you today is in furtherance of that word of encouragement.

As president of ServiceMaster and as a member of the board of the National Committee on Quality Health Care, I am interested in seeing that the Federal sector has available to it the same programs and benefits found to be effective in the private sector. It is not necessary to conduct a \$10 million to \$20 million survey in order for the VA to consider these benefits. The Air Force already has proven what the private sector also has found, namely that the costs of survey and analysis typically are borne by those who desire to deliver services. The competitive nature of the marketplace allows the customer to consider the best alternative -- including a fair comparison of the alternative of in-house management -- without significant cost to the institution.

We support and concur with the President's statement in signing PL9766, that the application of OMB Circular A-76 can result in substantial savings for the VA, with no degradation of patient care. We suggest that the VA undertake a pilot program, involving a responsible and responsive management firm serving a select group of VA hospitals, to determine the benefits of supporting management services for housekeeping, plant operations and maintenance, and food service, as an alternative to the present in-house programs. The results of this pilot program should be reported to this Committee, with further consideration regarding whether such a program should have VA system-wide application.

Thank you.

SPECIAL SECTION

CONTRACT MANAGEMENT SURVEY

Department management rose 12.7% during 1980

By Vince DiPaolo
Managing Editor

Some 4,079 hospital and healthcare facility departments were managed full-time by outside contractors in 1980, a 12.7% increase over 3,618 departments in 1979, MODERN HEALTHCARE's second annual survey of leading department managers found.

Almost all department managers cited cost containment pressure on hospitals and all healthcare facilities as the primary motivation for farming out clinical and non-clinical services to department management firms.

The rate of increase in departments turned over to outside management wasn't as large as the 14% rise reported between 1975 and 1979 in MODERN HEALTHCARE's first survey (MH, August 1980, p. 57). But a defi-

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Distribution of contracts

Service	Change	Number of clients		Contractors reporting	
		1980	1979	1980	1979
Housekeeping	+ 8.5%	1,099	1,013	6	2
Food service	+ 9.0%	1,033	961	11	10
Respiratory therapy	+ 11.7%	574	514	11	10
Plant operations/maintenance	+ 11.0%	283	258	5	5
Pharmacy	+ 24.1%	279	227	8	7
Laundry	+ 12.7%	258	229	7	7
Physical therapy	+ 18.3%	142	120	3	3
Data processing	+ 11.0%	131	118	10	11
Alcoholism treatment	+ 31.1%	68	51	3	2
Cardiopulmonary diagnostics	+ 43.4%	56	39	2	1
Biomedical engineering	+ 14.1%	48	42	2	2
Materials management	+ 25.0%	39	31	5	4
Other services	+ 37.0%	53	44	17	10
Totals	+ 12.7%	4,079	3,618	92	80

Modern Healthcare/July 1981

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Survey

Continued from page 73
nite trend toward outside management continues in the industry.

For our survey, department management is defined as having a person on the payroll of a management firm working full time managing a department of a hospital or healthcare facility. Departments managed as part of total hospital or healthcare facility management contract aren't included in our survey.

Housekeeping remains the service most frequently contracted for, accounting for 26.9% of all managed departments reported in our survey. Food service is next with 25.8%, followed by respiratory therapy with 14.1%.

Pharmacy departments showed the largest percentage increase in outside management among those services most frequently contracted out. Managers operated 270 departments last year, up 24.4% from 217 in 1979. Materials management department managers added eight departments for a 25.8% gain, but their total, 39 de-

Continued on page 76

	No. of contracts		No. of services	
	1980	1979	1980	1979
ServiceMaster Industries Downers Grove, IL	1,303	1,209	5	5
ARA Services Philadelphia, PA	282	246	2	11
Orhalation Therapy Services Lexington, MA	229	220	1	2
Custom Management Corp. Kingston, PA	189	143	3	3
Morrison's Management Svcs. Mobile, AL	181	169	2	2
American Management Svcs. Englewood, CA	165	150	3	4
Crothall International Newark, DE	148	120	4	3
Respiratory Care Services Jackson, MS	137	95	2	1
SAGA Corp. Menlo Park, CA	127	119	1	1
HRI Hospital Pharmacies Inc. Los Angeles, CA	123	112	1	1
Physical Therapy Associates Wharton, TX	120	110	1	2
Marriott—Business & Professional Services Div. Washington, DC	96	86	2	2
Fogd Dimensions, Inc. San Francisco, CA	86	78	1	1
American Intermedical Rsrchs. Birmingham, AL	79	57	1	1
The Owen Company Houston, TX	64	51	1	1
Comprehensive Care Corp. Newport Beach, CA	64	50	2	2
Lifemark Auxiliary Services Houston, TX	55	44	3	3
National Medical Enterprises Los Angeles, CA	52	52	1	1
Hospital Dietary Services Farmington Hills, MI	50	56	1	1
Service Directions Inc. Minneapolis, MN	49	46	1	1
CompuCare Inc. McLean, VA	44	39	1	1
Medicus Systems Evanston, IL	39	37	2	2
IHP Corp. Oklahoma City, OK	35	29	4	4
Greene & Kellogg, Inc. Tonawanda, NY	34	41	1	1
CuraCare Inc. Mobile, AL	32	25	1	1
Cuisine Management Svcs. Emmaus, PA	30	30	1	1

MODERN HEALTHCARE (APRIL/JULY 1981)

Table 3 Percentage distribution

Service	1980	1979
Housekeeping	26.9%	28.0%
Food service	25.8%	26.6%
Respiratory therapy	14.1%	14.2%
Plant operations/maintenance	5.9%	7.0%
Pharmacy	5.5%	5.0%
Laundry	6.3%	5.3%
Physical therapy	3.5%	3.3%
Data processing	3.2%	3.3%
Alcoholism treatment	1.7%	1.4%
Cardiopulmonary diagnostics	1.4%	0.6%
Biomedical engineering	1.2%	1.2%
Materials management	1.0%	0.8%
Other services	1.4%	1.2%

MODERN HEALTHCARE (APRIL/JULY 1981)
contracts(1) contracts(1)

Table 4 Housekeeping services

	No. of clients		No. of states	Year started
	1980	1979		
ServiceMaster Industries Downers Grove, IL	788	743	46	1962
American Mgmt. Svcs. Englewood, CO	126	114	32	1959
Crothall Hospital Services Newark, DE	113	102	26	1969
Custom Management Corp. Kingston, PA	31	21	6	1974
Harry A. Stich Associates Princeton, NJ	27	18	15	1951
Triplett Services Farmington Hills, MI	6	8	1	1973
Morrison's Mgmt. Svcs. Mobile, AL	3	2	1	1979
Marriott Bus. & Prof. Div. Washington, DC	5	5	3	1974
Totals	1,059	1,013		

MODERN HEALTHCARE (APRIL/JULY 1981)

Table 5 Laundry services

	No. of clients		No. of states	Year started
	1980	1979		
ServiceMaster Industries Downers Grove, IL	178	173	38	1965
American Mgmt. Svcs. Englewood, CA	29	21	11	1972
Crothall Hospital Services Newark, DE	25	10	15	1978
Mediq Inc. Parsippany, NJ	9	9	2	1974
Custom Management Corp. Kingston, PA	8	5	3	1974
Triplett Services Inc. Farmington Hills, MI	6	8	1	1973
Foussard Associates St. Paul, MN	3	2	3	1971
Totals	258	229		

MODERN HEALTHCARE (APRIL/JULY 1981)

Survey

Continued from page 74

partments, accounted for less than 1% of all the departments under contract.

Food service and respiratory therapy services had the largest number of providers, 11 each, and there were eight providers for both housekeeping and pharmacy services.

■ ServiceMaster Industries, Downers Grove, IL, remains by far the nation's largest department manager, providing five services to 1,303 hospital departments in 1980, up 7.8% from 1,209 departments a year earlier. Overall, ServiceMaster accounted for

almost 32% of all the departments managed by the 60 firms responding to

Cost containment pressure is a primary reason why hospitals are farming out management of some clinical and support services

this year's MODERN HEALTHCARE survey.

ServiceMaster is the largest housekeeping department manager with 788

clients, up 6% from 1979. It also is the leader in providing laundry department management, 178 clients; biomedical engineering, 47 clients; materials management, 32 clients; and plant operations and maintenance, 258 clients.

The second largest department manager is ARA Services, Philadelphia, with 282 departments managed, up 14.6% from 1979. Other leading department managers include Inhalation Therapy Services Inc., Lexington, MA, 239 clients; Custom Management Corp., Kingston, PA, 189 clients; and

Continued on page 78

Plant operations & maintenance services

	No. of clients		No. of states	Year started
	1980	1979		
ServiceMaster Industries	258	227	41	1970*
Downers Grove, IL				
American Management Svcs.	10*	14	8	1977
Englewood, CO				
Croftall Systems	8	8	5	1975
Newark, DE				
Toplett Services Inc.	5	5	1	1973
Farmington Hills, MI				
Harry A. Strub Associates	2	1	1	1979
Princeton, NJ				
Totals	283	255		

MODERN HEALTHCARE chart July 1981

Food services

	No. of clients		No. of states	Year started
	1980	1979		
ARA Services*	269	246	42	1952
Philadelphia, PA				
Marrison's Mgmt. Svcs.	178	167	16	1952
Mobile, AL				
Custom Management Corp.*	150	116	16	1968
Kingston, PA				
SAGA Corp.	127	119	NA	1963
Monte Park, CA				
Mannett Business & Professional Services	91	81	26	1955
Washington, DC				
Food Dimensions Inc.	88	78	4	1972
San Francisco, CA				
Hospital Dietary Services	50	56	6	1965
Farmington Hill, MI				
Service Directions Inc.	49	46	10	1969
Minneapolis, MN				
Cuisine Mgmt. Svcs.*	30	30	2	1981
Emmery, PA				
Stouffer Food Svcs. Div.	21	22	5	1981
Solon, OH				
Croftall Food Services	2	0	2	1980
Newark, DE				
Totals	1,053	961		

* This business unit includes dining halls and retirement centers and 100 of Custom Management's health and hospital departments including the Metro-City, Cleveland, OH, effective May 31. Custom Management has 100 contracts with nursing homes.

MODERN HEALTHCARE chart July 1981

Table II Respiratory therapy

	No. of clients		No. of states	Year started
	1980	1979		
Inhalation Therapy Svcs.*	239	220	36	1963
Lexington, MA				
Respiratory Care Services	105	95	16	1971
Jackson, MS				
American Intermedical Res.	79	57	20	1972
Birmingham, AL				
National Medical Ent.	52	52	11	1971
Los Angeles, CA				
Greene & Kellogg	34	41	6	1945
Tonawanda, NY				
Cura Care Inc.	32	25	9	1974
Mobile, AL				
Lifemark Ancillary/Services	21	17	14	1972
Houston, TX				
Eskaton	5	3	1	1978
Carmichael, CA				
St. Luke's Medical Center	3	3	1	1979
Sioux City, IA				
IHP Corp.	3	1	1	1979
Okishoma City, OK				
St. Elizabeth's Health Ctr.	1	0	1	1980
Lincoln, ND				
Totals	574	514		

* Physical Therapy Associates is subsidiary of Health Systems Management Corp. (HSM) which acquired the company after AM bought Health last year.

MODERN HEALTHCARE chart July 1981

Table III Materials management services

	No. of clients		No. of states	Year started
	1980	1979		
ServiceMaster Industries	32	25	18	1975
Downers Grove, IL				
Medig Inc.	3	3	1	1974
Pennington, NJ				
Henry Ford Hospital	2	2	1	1979
Detroit, MI				
Health Central Inc.	1	0	1	1980
Minneapolis, MN				
Pharmaco Inc.	1	0	1	1980
Lubbock, TX				
Totals	39	31*		

* American Management Services is contracted materials management services in 1980. It had one client in 1979.

MODERN HEALTHCARE chart July 1981

Survey

Continued from page 78

Morrison's Management Services, Mobile, AL, 181 clients.

ARA is the leading food service department manager with 269 clients. Inhalation Therapy Services is the

leading respiratory therapy department operator with 239 clients. Hospital Pharmacies Inc., Los Angeles, is the leader among pharmacy management firms with its 123 clients.

Physical Therapy Associates, Wharton, TX, with 120 clients, is the leading manager of physical therapy departments in healthcare institutions. Comprehensive Care Corp., Newport Beach, CA, leads

the nation in managing alcoholism treatment units in hospitals with 60 clients.

A shortage of nurses and virtually every other type of medical professional and technician except physicians will create an increased demand for clinical department management services. Such department management firms usually recruit health professionals to staff their managed facilities.

Physical therapists, for example, are in greater demand because federal law now requires each school district that teaches handicapped children to keep a

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Table 10 Pharmacy management

	No. of clients		No. of states	Year started
	1980	1979		
HPI Hospital Pharmacies Los Angeles, CA	123	112	30	1967
The Owen Co. Houston, TX	64	51	16	1970
Pharmaceuticals Mgmt. Inc. Los Angeles, CA	22	7	3	1973
Lifemark Ancillary Services Houston, TX	19	22	10	1976
Medical Products Systems Bartlesville, OK	19	12	2	1972
Pharmacy Systems Inc. Columbus, OH	15	11	5	1973
Pharmaco Inc. Lubbock, TX	6	1	1	1979
Henry Ford Hospital Detroit, MI	1	1	1	1977
Methodist Hospital Memphis, TN	1	0	1	1980
Totals	270	217		

MODERN HEALTHCARE
Chart, July 1981

Table 11 Financial management svcs.

	No. of clients		No. of states	Year started
	1980	1979		
Brim & Associates Portland, OR	7	6	4	1973
Methodist Hospital Dallas, TX	1	2	1	1979
Metropolitan Hospitals Portland, OR	2	1	1	1976

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MODERN HEALTHCARE Chart, July 1981

Survey

Continued from page 78

physical therapist on staff. This, and the fact that many physical therapists are setting up independent private practices, has greatly reduced the manpower pool available to staff hospital PT positions, says Tom Carlson, president of Physical Therapy Associates.

■ "We now have 135 PTs on staff and we could use 25 more, but we can't get them even though we pay the highest

wages in the industry," Mr. Carlson says.

Industry sources estimate there are 40,000 practicing physical therapists and an unmet demand for 8,000 more.

Ever escalating pressure from government to keep healthcare costs down is one reason many hospitals and nursing homes are turning to outside department managers, says Graeme Crothall, president of Crothall International, Newark, DE. Crothall provides

housekeeping, laundry, plant operations and maintenance, and food service management to 148 hospital departments.

"People are becoming more familiar with the concept of department management and thus are more willing to contract out support services so a hospital can concentrate its energies on its main purpose—healing the sick," says Mr. Crothall. Where before only small hospitals would contract out management of a department, today many teaching hospitals are doing the same, he says.

Pharmacy department management arrangements are changing from predominantly revenue-sharing between the manager and the hospital to flat-fee agreements, according to Chuck Augello, Pharm.D., vice president for operations, Pharmaceuticals Manage-

A shortage of professionals and technicians will increase demand for clinical department management

ment Inc., Encino, CA. The state of California passed a law that requires all new contracts to be based on fee arrangements and requires all previously existing revenue-sharing contracts to be phased out by 1986. Other states are considering similar legislation.

Some department managers are developing multiyear consulting relationships where the management firm initially takes over complete management of a department but eventually trains hospital employees to operate the facility, thus phasing the consultant out of the job.

"Contract services have to be more flexible," says Wallace Leary, director of marketing services, American Management Services, Englewood, CO. AMS manages housekeeping, laundry and plant operations and maintenance services for 165 departments.

However, traditional department management arrangements are still in vogue in many services. "I haven't seen any of that (consulting arrangements) happening in food service," says Mary Beth Crimmins, vice president for hospital food management with ARA.

ARA, however, when requested, will provide consulting services to a department management client. "We have looked at the possibilities of consulting contracts, but our main business lies in managing dietary departments." ■

Survey

Other services *Continued from page 78*

	No. of clients		No. of states	Year started
	1980	1979		
<i>Physical therapy services</i>				
Physical Therapy Assocs. ^A	120	110	26	1963
Wharton, TX				
Lifemark Ancillary Svcs.	15	5	10	1978
Houston, TX				
IHP Corp.	7	5	1	1976
Oklahoma City, OK				
<i>Alcoholism treatment svcs.</i>				
Comprehensive Care Corp.	60	48	24	1973
Newport Beach, CA				
American Intl. Health Svcs.	7	3	5	1976
Worcester, MA				
Geisinger Medical	1	0	1	1980
Management Corp.				
Danville, PA				
<i>Cardiopulmonary diagnostic services</i>				
Respiratory Care Svcs.	32	0	5	1980
Jackson, MS				
IHP Corp.	24	23	1	1971
Oklahoma City, OK				
<i>Biomedical engineering svcs.</i>				
ServiceMaster Ind.	47	41	17	1976
Downers Grove, IL				
Triplet Services Inc.	1	1	1	1978
Farmington Hills, MI				
<i>Management engineering</i>				
Medicus Systems	16	15	9	1970
Evanston, IL				
Health Central Inc.	1	0	1	1980
Minneapolis, MN				
<i>Management training svcs.</i>				
Henry Ford Hospital	2	2	1	1979
Detroit, MI				
Pacific Health Resources	1	1	1	1980
Los Angeles, CA				
<i>Radiology services</i>				
Geisinger Medical	2	0	1	1980
Management Corp.				
Danville, PA				
St. Elizabeth's Health Cntr.	1	0	1	1980
Lincoln, NB				
<i>Psychiatric services</i>				
Mental Health Mgmt.	3	2	3	1979
Washington, DC				
Comprehensive Care Corp.	4	2	4	1974
Newport Beach, CA				
<i>Nursing services</i>				
Janna Medical Systems	2	0	2	1980
St. Louis, MO				
<i>Emergency medical svcs.</i>				
Geisinger Medical	1	0	1	1980
Management Corp.				
Danville, PA				
<i>Medical records services</i>				
Henry Ford Hospital	1	1	1	1977
Detroit, MI				
<i>Occupational therapy svcs.</i>				
IHP Corp.	1	0	1	1980
Oklahoma City, OK				
<i>Dialysis services</i>				
Dialysis Management Int.	4	4	4	1979
Littleton, CO				
<i>Clinical laboratory svcs.</i>				
International Clinical Labs	9	8	5	1970
Nashville, TN				

^A—Inhalation Therapy Services, Physical Therapy subsidiary, which had 4 contracts, was merged into Physical Therapy Associates when AMT bought Hyatt last year.

MODERN HEALTHCARE chart July 1981

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magazine.

ServiceMASTER

Action

CONTINUAL EFFORTS AT HOSPITAL COST CONTAINMENT

by Illinois Congressman Dan Rostenkowski,
Chairman, Subcommittee on Health of the
Committee on Ways and Means



I am pleased to have the opportunity to participate in the ServiceMaster Award of Excellence program. My remarks will focus on an issue that is important to me as a legislator and to you as a major force in the delivery of health care services—the Center Administration's continuing efforts to enact a hospital cost containment program.

First, I would like to commend your organization for bringing about a more organized and therefore more efficient delivery of health care services in the more than 600 institutions currently employing your talents. Recently there came to my attention a publication from a New York brokerage house which stressed the strong prospects for your company. To quote from the report: "We note that the firm meets our often repeated criteria of providing services that increase hospitals' productivity and efficiency." I am gratified that even the Wall Street analysts perceive the need to stress greater efficiency and productivity in the delivery of health care.

Naturally, I am extremely pleased that an Illinois-based company such as ServiceMaster has acquired a reputation for excellence in the pursuit of that goal.

Congress is beginning what I would describe as a second phase in drafting cost containment legislation. Whether or not this congressional session will be marked by a mere continuation of last year's effort, or bring a fresh and different approach, is yet to be seen.

SETTING HEALTH CARE PRIORITIES

I share the view that it is imperative to arrive at a public policy that will permit all of us—those in the private, as well as in the public sector—to work toward the management of rising hospital costs.

Last year my Subcommittee conducted an extensive and critical assessment of the effectiveness and acceptability of the Administration's cost containment proposal. That the Subcommittee has devoted so much time to the bill without arriving at a consensus strongly indicates, I believe, that major modifications may be necessary to assure passage of the Administration's program. But, before I say more about this year's prospects, we need to discuss what has brought us to seriously consider such comprehensive and far-reaching legislation.

How ironic that after years of heated debate about how to expand the availability of services, we find ourselves much concerned about controlling rising health costs by curtailing demand. The irony is compounded by the fact that instead of urgent calls to deal with unmet health care needs, we hear much more about excessive capacity and unnecessary use of services.

I am not yet prepared to judge the wisdom of this new outlook. I confess to a degree of difficulty in adjusting to the shift in emphasis. Accessibility to medical care—including medical advances from research—is a vitally important to every individual. Many of our citizens still cannot afford necessary medical care. Whatever views are expressed about the relative value of medical care in achieving the good life, it is something that every individual perceives as essential to his well-being. I believe, therefore, that despite our current anguish over costs, some form of national health insurance is a matter of high priority.

Nevertheless, I am also prepared to recognize, as a member of the Committee that must find the way to finance such a program, that the steadily rising cost

The Honorable Dan Rostenkowski, United States Congressman from Illinois' 8th District, was elected to the House of Representatives in 1958. He has served in each succeeding Congress, and has held several positions relating to health care and monetary policy.

Elected to the House Ways and Means Committee in 1964, Congressman Rostenkowski was chairman of the Subcommittee on Health for the 94th and 95th Congresses. He has also been a member of the Joint Committee on Taxation and the Steering and Policy Committee, as well as Chief Deputy Majority Whip for the 95th Congress. He sponsored legislation creating a new system of Congressional budgetary controls while a member of the 93rd Congress' Joint Study Committee on that subject. Congressman Rostenkowski is a graduate of Loyola University.

His remarks are excerpted from a recent presentation to a ServiceMaster Industries Inc. Management Group.

of health care services is an issue that cannot be ignored or minimized. The intense competition for available dollars—federal as well as private dollars—compels us to reassess what were until recently accepted premises and goals in this area of public policy.

Virtually everyone agrees on the need to devise effective measures for restraining the rising cost of hospital care before the enactment of national health insurance. While this may sound harsh to many people who have repeatedly urged immediate enactment of national health care insurance, it is a position based on realistic assumptions.

THE DANGERS OF HASTY ACTION

Accepting this need to face up to the issue as a matter of public priority, the appropriate Committees of the last session of Congress moved to consider the Administration's proposed remedy. In reviewing these efforts, two major points become evident to me.

First, it is clear that there was a mood of profound impatience on the part of the Administration in asking for the immediate enactment of their hospital cost containment proposal. It would be misleading to minimize or discount the pressure generated by the Administration to quickly decide upon and adopt a course of action. However, the members of my Subcommittee felt that we needed to thoroughly examine the implications of this or any other proposal to contain hospital costs. For example, it is our responsibility to be sure that any proposal does not penalize those institutions (such as many of your clients) who are already making conscientious efforts to improve productivity in the delivery of health care services. If our long-run goal is efficient health care, we have to be sure we are not inadvertently compromising or jeopardizing that goal while pursuing the short-run objective of containment of hospital costs.

Second, it became clear that we must be aware of the pitfalls in any attempt to deal hastily with a problem as complex as hospital costs. For example, we must guard against the tendency to overlook the implications of the approach adopted for other aspects of the health care system, or the inclination to minimize the enormous economic and political obstacles to enacting an effective policy. Equally important, there is the danger of implying that the problem exists only because of a reluctance of all parties to work together for a reasonable solution.

I have sought to dissipate what appeared to be a growing resentment and belligerence between the public and private sectors. To help clear away some of the resistance to a more cooperative and responsible approach to the issue, I invited the health industry to

contribute their ideas for attacking the cost problem. My statement was not intended as an either/or challenge—either a voluntary approach showing immediate results, or a federally-imposed solution. That's neither fair nor reasonable. What I sought was action by the industry to identify possible measures to help achieve the goals I believe we all share—cost-effective use of our resources without impairing public access to needed services. I was encouraged by the industry's response, particularly its unequivocal recognition that we do have a serious problem, and that effective action to deal with the problem is both necessary and urgent. But I trust that it is equally clear that such an invitation carries with it no commitment on the part of Congress to delay consideration of pending legislation. What it does imply is that the industry has an opportunity to help shape what emerges from these deliberations through the contributions it can make to the legislative process, as well as by any actions it takes to promptly implement effective nationwide voluntary measures.

THE MIDDLE GROUND OF COST CONTROL

Let me be misunderstood, let me say that like many others, I would like to see Americans—private industry no less than individuals—do more for themselves and expect less to be done for them by government. But I am also aware that Americans continue to believe that a great many problems require, if not the wholesale intervention of government, at least its participation. And it seems to me that in the health field the federal government must be involved. The scope and extent of that involvement now seems the crux of the issue.

After briefly analyzing the preliminary proposals of the National Steering Committee for Voluntary Cost Containment organized by the American Hospital Association, the Federation of American Hospitals, and the American Medical Association, I am encouraged to note several areas of similarity between what has been advocated by the Administration and what the industry would accept.

First, in the development of a voluntary effort, I see strong recognition that something must now be done to address the cost issue. The voluntary effort even has proposed reducing the rate of increase in hospital costs to approximately 11.7 percent for 1978. This is quite compatible with the 10.9 percent aggregate revenue cap of the Administration's proposal when all its exceptions and pass-throughs are computed into the limit.

Although no one likes flat per admission revenue increase limitations as a long-range solution to the control of health care costs, this endorsement of such limits as an interim

solution by the hospital industry might help break the impasse that has retarded consideration of the cost bill.

The voluntary effort has also recognized the relationship of unrestrained capital growth to cost inflation. Their advocacy of a national limit on new capital expenditures follows closely the philosophy of Title II of the Administration's bill. The voluntary proposal, which as I understand calls for no national net increase in beds as well as a reduction in the rate of capital growth, is also a move toward middle ground.

Thus, the Administration and the industry are not that far apart on their goals. What is needed is an acceptable compromise on the ways to attain those goals. This is the challenge that lies before us.

DIFFICULT QUESTIONS TO ANSWER

As we in Congress continue to give and take on the issue of hospital costs, there are several broad policy questions—in a sense, philosophical questions—that must be kept in mind. These questions go beyond the limited proposition of a temporary cap on revenues.

For instance, do we want health care costs in the future to rise in line with the general growth of the economy? Or is there another more appropriate standard that ought to be applied to the health industry? How much innovation and new health care technology can we manage? Is it really possible to exert more control over health technology costs while maintaining, and even enhancing, the quality of care delivered? How can we reconcile a policy aimed at reducing use of health services with the fact that millions of Americans are still underserved by the health care sector?

It is one thing to have these questions in mind; quite another to provide satisfactory answers. I don't believe there are any definitive answers yet.

I hope that in the months ahead both the Administration and the health care industry will demonstrate enough flexibility to institute a cost containment strategy that will be fair, manageable, and will bring a measure of fiscal relief to all who must purchase health care.

As a company that has made increased health care efficiency its business, I know that you at ServiceMaster will continue to participate in this process. And as a company whose business interests lie between the basic providers and purchasers of health care, you are in a unique position to help bring the health care industry and government closer together in an alliance that benefits all.

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Downers Grove, Illinois 60515

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RESPONSE OF SERVICEMASTER INDUSTRIES INC. TO WRITTEN QUESTIONS SUBMITTED BY HON.

ALAN K. SIMPSON, CHAIRMAN OF THE SENATE COMMITTEE ON VETERANS' AFFAIRS

- Q.1 Can you provide the Committee with profit margin figures from your company on the work you do in private hospitals?
- A. In 1980 ServiceMaster reported a 3.3% after tax profit margin on revenue from health care services and other operations. This is consistent with margins earned over the past several years.
- Q.2 Do you expect any change in the duties performed or your profit margin in contract work performed for the VA's Department of Medicine and Surgery?
- A. Our management programs begin with a basic system which is adapted to meet the specific needs of the individual hospital. In the contracting process we work with hospital administration to determine the program required for the facility. These requirements then are described in a detailed performance agreement which includes both quality standards and guaranteed cost. We would expect to follow a similar procedure in working with Veterans Administration hospitals, designing a management program for each VA facility based on the statement of work outlined by the administration of that hospital. We also would expect to hold to our current profit margin, which we feel allows us to be competitive in serving hospitals in the private sector as well as Federal Government facilities.
- Q.3 What is the average duration of your contract relationships with private hospitals? What is your rate of renewal and your rate of contract termination, including, if available, the reasons for such termination or nonrenewal?
- A. Our renewal rate, on average, over twenty years of experience serving in health care is better than 90%. Hospitals have rarely terminated their relationship with us prior to the end of a contract period. Where our contract with a facility has not been renewed, it generally has been for one of three reasons?

- 1) The hospital has decided to return to in-house management. This most often occurs during a change in hospital administration, where a new administrator is brought in who is opposed to the concept of contract management, and does not have a perspective of what we have achieved for the facility in cost containment, quality improvement, and better management control.
- 2) ServiceMaster elects to terminate a relationship, usually because of the hospital's failure to pay for our services in a timely fashion.
- 3) The hospital judges our performance unsatisfactory, or another service firm underbids us.

Q.4 Can you provide the Committee with figures comparing the housekeeping costs at VA hospitals with those at private hospitals?

A. Veterans Administration hospitals reportedly spend an average of 6% of their operating budget for what is termed "building management", which consists primarily of housekeeping functions. In the private sector hospitals spend an average of 3% or less of their budgets for housekeeping services.

Q.5 What is the extent of your experience with contracts mandated by A-76?

A. Despite the directive of A-76, to our knowledge Federal Government hospitals generally have not opened up to supporting management services such as we provide. The only exception to this is Air Force hospitals, which began contracting with firms such as ours before the recent attention given Circular A-76.

Q.6 Please describe the specific extent of ServiceMaster's relevant contract experience with Air Force hospitals?

A. In 1975 ServiceMaster became the first service management firm to work with the Air Force in its Hospital Aseptic Management Program. Since then we have bid successfully to

serve at various times in 15 Air Force facilities. At the present time we provide housekeeping services in five Air Force hospitals, and will introduce our program in eight additional facilities in 1982. ServiceMaster has experienced only one termination of an Air Force contract. This was due to a dispute over terms of the contract and the scope of services to be provided. On the other hand, we have renewed our contracts with a number of Air Force facilities during the cyclical bidding process.

- Q.7 In your dealings with DOD, what percentage of displaced Federal employees have you rehired and how does your pay scale, including fringe benefits, compare with that of the Federal Government?
- A. Our experience has been primarily in situations where the government hospital was served previously by a contract management firm. In these cases displaced employees already were part of the private sector. We have taken over management of only one housekeeping department in which the staff was made up entirely of government civil service employees. In that instance we filled more than 90% of our staff positions with Federal employees previously on the in-house staff.

Regarding pay scale and other compensation, ServiceMaster follows the U.S. Dept. of Labor's Register of Wage Determination, which indicates what the average worker receives in wages and benefits for a specific job category in the community in which the Government hospital is located. These Wage Determination averages are generally below the rate paid to civil service employees, but well above the Federal minimum wage. In 1976, for example, the Wage Determination rates for employees we managed in Air Force hospitals averaged 24% less than the average rate paid civil service employees, and 35% more than the Federal minimum wage. In 1981 our Air Force hospital housekeeping workers are paid an average of 10% less than similar workers in civil service jobs, and 55% more than the Federal minimum wage requirement.

RESPONSE OF SERVICEMASTER INDUSTRIES INC. TO WRITTEN QUESTIONS SUBMITTED BY HON.

ALAN CRANSTON, RANKING MINORITY MEMBER OF THE SENATE COMMITTEE ON VETERANS'

AFFAIRS

- Q.1 Please provide for the record information as to the number of government hospital facilities at which your members have had contracts for cleaning over the past three years and the instances in which there have been work interruptions for all causes, such as strike, bankruptcies, contract defaults, and the like.
- A. In the past three years ServiceMaster has initiated or renewed 14 contracts for housekeeping services with Air Force hospitals. We have experienced no interruption of service at any of these hospitals during this period. In fact, with the exception of the single termination described in the answer to Question Two, we have experienced no interruption of service in any Air Force hospital since we began serving these facilities in 1975.
- Q.2 Have any of the contracts which your organization has had with the Federal Government or medical facilities been terminated? If so, why was the contract terminated? How many such contracts have been terminated?
- A. ServiceMaster has experienced only one termination of a contract with a Federal facility. This occurred in 1977 at one of the Air Force hospitals, and was due to a dispute over terms of the contract and the scope of services to be provided.
- Q.3 On a percentage basis, how many displaced government employees do you ordinarily hire when you receive a government contract for commercial or industrial type activities?
- A. Our experience has been primarily in situations when the Government hospital was served previously by a contract management firm. In these cases displaced employees already

were part of the private sector. We have taken over management of only one housekeeping department in which the staff was made up entirely of civil service employees. In that instance we filled more than 90% of our staff positions with Federal employees previously on the in-house staff.

Q.3B When you hire these employees, do you make any special efforts to give a preference to veterans?

A. ServiceMaster follows Federal guidelines for equal opportunity employment in all of its hiring policies both in the private sector and in Government hospitals.

Senator DECONCINI. Mr. Daoust.

Mr. DAOUST. Mr. Chairman.

I'm George Daoust, executive director of the National Council of Technical Service Industries, an association of 25 companies, all of whom do a considerable amount of work for the Government.

I also represent the Committee on Contracting Out, a group of 25 associations and councils—NCTSI is one of them. Its membership exceeds 25 million workers, a great many of whom are veterans working on A-76 type contracts for the Federal Government.

Copies of the membership list are attached to my written testimony, which I should like to have entered into the record.

Senator DECONCINI. Without objection, it will appear in the record.

Mr. DAOUST. Five minutes isn't much time to discuss the broad scope of issues this committee faces with regarding contracting out to the Veterans' Administration.

One thing is certain in my mind, however. Providing medical support for the veterans is not a governmental function. I spent 26 years in the Army and had two more as a political appointee in Defense, and had a fair idea of when I was involved in a Government function.

I wasn't doing any governing as a private, nor as a cadet; not when I was a lieutenant or a captain. I was on the Federal payroll doing military service, but not governing.

Now, as a field grade officer, I sometimes became involved in political military assignments that included governmental functions, and clearly so as a political appointee in Defense.

But no printer, programmer, carpenter, or plumber on the Federal payroll is performing a Government function; nor any doctor, nurse or medical technician performing medical care.

In the hearings on Public Law 97-66 last month, the March 21, 1980, decision of VA General Counsel was used to challenge the legality of contracting out basic medical care operations.

NCTSI's counsel, Arnold and Porter, has looked into this matter, and has given us their view that the opinion of the VA General Counsel is an incorrect application of OMB Circular A-76. Copies are attached to my written testimony.

There is a wealth of material from the GAO this year on the value to the Government of contracting out. They have also identi-

fied a lot of the problem areas, and almost all involving the neglect, incompetence, or complicity of Government procurement officials.

These derelictions should not be used to justify keeping work in-house. If the spotlight's turned on poor governmental management practices in connection with contracting, it behooves us to look into the overall effectiveness of Government in commercial industrial activities, not the minor role of the contractor.

Similarly, in the Senate discussion of Public Law 97-66, the issue of striking was raised. This seems incongruous in the year of PATCO. But suffice to say industry is as responsible as Government in getting its job done. The Boeing Co. worked around a strike at Cocoa Beach at the time of the last launch, with no adverse effects on the space shuttle.

With respect to the Veterans' Administration, all industrial and commercial-type activities should be examined for cost effectiveness, including medical and technical services.

The doctors and other medical professionals that cared for President Reagan after he was shot were not part of the governing function. They were medical professionals doing their job regardless of their lack of status as governmental employees.

Do we need another standard for our other veterans, or is all this discussion of governmental function a smokescreen to obscure the real issue—big Government?

Another question frequently raised is about the loss of jobs by Government employees.

When a Federal CITA function is put out for contract, some 85 percent of the employees are retained in their jobs. Do they then become less efficient, competent or dedicated? Quite the contrary. Nothing so saps performance as working in an overstaffed, under-supervised environment.

Circular A-76 requires that Government employees be given first option on jobs contracted out, and they take full advantage to do so. Working in the private sector isn't all that objectionable to most Americans. In fact, there are very few that don't work there before or after their governmental service.

Almost all of our veterans are in the private sector, used to and content with the free-enterprise system. In fact, if you query the veterans rather than the staff at VA facilities on how they would like more, better quality care, I imagine you would find strong support for competitive, industrial workers rather than bureaucracy. Government certainly has no monopoly on good, conscientious work. In fact, the very thought of this is humorous.

You may also ask, "How does such a service contract actually work?" With a contract that is properly negotiated and supervised, amazingly well. Take the service support contract let at Fort Gordon, Ga., on September 1, 1980. Of the 396 Government employees involuntarily separated, 380, some 96 percent went to work for Pan-Am, the contractor.

The cost of service orders in housing maintenance is one-half what it was under the Government. Food service is described by Army inspectors as better controlled and a better quality than it was before. Contract costs are running below estimates and the 3-year savings will be \$31.9 million.

Mr. Chairman, the thrust of my testimony is to not deny our veterans an opportunity for better, more-efficient, and less-expensive care. It is depressing to see an arbitrary prohibition on cost comparisons to find out what savings would occur for our veterans through both reductions in in-house staff during the efficiency review and by contracting out where it is cheaper. A-76 cost comparisons are working elsewhere in our Government to save hundreds of millions of dollars. Don't do less for our veterans and our taxpayers.

This Tuesday Mr. Stockman sent a letter to Senator Hayakawa, strongly supporting the use of OMB Circular A-76 for the commercial, industrial-type activities, and estimated a 5-year saving in excess of \$3 billion by 1987. I hope that this Committee will act to see that the Veterans' Administration shares in these savings.

Thank you.

Senator DeCONCINI. Thank you, Mr. Daoust.

[The prepared statement of Dr. George A. Daoust, Jr., executive director, National Council of Technical Service Industries, and the November 3, 1981, letter to Hon. S. I. Hayakawa, a U.S. Senator from the State of California, from David A. Stockman, Director, Office of Management and Budget, follows:]

PREPARED STATEMENT OF DR. GEORGE A. DAOUST, JR., EXECUTIVE DIRECTOR, NATIONAL
COUNCIL OF TECHNICAL SERVICE INDUSTRIES

Mr. Chairman, I am Dr. George A. Daoust, Jr., Executive Director of the National Council of Technical Service Industries (NCTSI). This testimony is presented on behalf of the twenty-five member companies of NCTSI, all of whom do a considerable amount of service work for the federal government. A list of our membership is attached. Most of these companies are deeply involved in OMB Circular A-76 contracting as well as providing the wide range of products and services to the private sector that has caused many of their names to become well known. We are greatly concerned by the provisions of S.917, the "Veterans Disability Compensation, Housing and Memorial Benefit Amendment of 1981"-which in Section 5010(a) forbids cost studies for contracting-out for commercial or industrial products and services unless funds have been specifically appropriated for that purpose. This is a very clever way to circumvent cost savings by the private sector - prevent the cost analysis and it doesn't matter what type of savings could be realized, the bureaucracy will continue unchallenged.

Mr. Chairman, I also represent the Committee on Contracting Out (COCO) a group of twenty five associations and councils, for which I am the Chairman of Legislation Affairs. A copy of the COCO membership roster is attached. These organizations have a membership in excess of 25 million workers in the private sector, many of whom work on projects for the federal government in accordance with the provisions of OMB Circular A-76.

There are so many errors in the agrumentation used in the Senate on October 1, 1981 to justify the position taken in Sec.

5010(a) that it is difficult to choose an issue on which to start. So, I'll begin with the basic, the concept of what is a governmental function? According to the provisions of OMB Circular A-76, governmental functions can only be performed by government employees.

On this there is general agreement. But, is cooking meals for veterans a governmental function? Mowing the lawn at a veterans hospital or operating on a veteran, or even on the President of the United States is clearly not a governmental function. These actions are paid for by the American-taxpayer, but we foot the bill for a lot that has nothing to do with the governing function.

The doctors and other medical professionals that cared for President Reagan after he was shot were not part of the governing function. They were medical professionals, doing their jobs regardless of their lack of status as governmental employees. Do we need another standard for our other veterans, or is all of the discussion of governmental functions a smoke screen to obscure the real issue - big government? If anyone really believes that the Congress has directed that only government employees can administer to the health requirements of our veterans, including providing food services, then that is the problem that should be addressed, and the law recinded.

Mr. Chairman, this issue is quite clear and is certainly central to contracting-out under OMB Circular A-76. If the preparation of food is considered to be a governmental function, regardless of for whom it is cooked, we have a major problem. Nothing is more basic to individual existence than eating. And

yet in a letter to you of Sept. 22, 1981 five members of this committee have linked the very doubtful opinion of the VA General Counsel of March 21, 1980 to food services so as to challenge the legality of having anyone but a bureaucrat prepare food for a veteran!

Our NCTSI Counsel, Arnold Porter, is pursuing the validity of this March 21, 1980 VA General Counsel opinion, and a copy of their initial conclusions is attached. To have passed Sec. 5010(a) on the basis of such a weak legal opinion is unfortunate.

Once this cloud is dispersed, the facts about cost savings through implementation of OMB Circular A-76 can emerge. The first is that whenever an A-76 cost comparison occurs there are savings. Whether or not the contract is let to the private sector, the realignment of the bureaucracy that is required before costing creates savings. In the Department of Defense a recent analysis of cost comparisons under OMB Circular A-76 show that a 20% savings occurs in the in-house expenses when the function under study is "organized and staffed for the most efficient performance" (as required by Circular A-76). This saving alone, if it proved to be more cost efficient to perform all VA work in-house, would pay for the cost comparisons and give the American taxpayers a dividend every year thereafter.

However, throughout the government there are substantial savings realized when commercial and industrial activities are performed by the private sector. In FY 1979 and 1980 the Department of Defense contracted for 60 conversions to industry at a cost of \$228 million. The in-house estimate for this work was

\$495.9 million giving a saving of 54% by contracting-out. Shouldn't the Veterans Administration share in such cost savings? Doesn't the taxpayer have a right to similar savings in the VA program?

In FY 1980 the Veterans Administration made 70% of its total procurement actions through noncompetitive process, the highest percentage of any major department or agency in the federal government. Denying the VA funds to conduct the cost comparisons for competitive contracting will not help this situation. The Office of Management and Budget identified 22,800 personnel spaces in the VA as having a potential for Circular A-76 cost comparisons in FY 1981. If one fifth of these spaces can be eliminated by the restructuring for cost comparison the saving will be great. If a further 20% to 50% saving can be made on the functions contracted-out there will be a dramatic reduction in costs for the VA.

The advantages to the government in contracting-out for services have been described in a series of General Accounting Office (GAO) reports this year. These reports answer many of the unfounded and emotional criticisms levied on the private sector during the Senate hearings on S.917. For example, in the GAO report "The General Services Administration Needs to Improve Its Cleaning and Guard Contracting Activities" of March 11, 1981 it is obvious that poor administration on the part of the GSA is the major problem. The GAO recommended that the Administrator of General Services "use competitive procurement procedures regardless of whether formal advertising or negotiation is used."

The GAO report "Civil Servants And Contract Employees: Who Should Do What For The Federal Government?" of June 19, 1981

contains the conclusion that "Federal agencies...use Government employees to provide commercial services that contractors could provide in many cases at a lower cost." There is an excellent GAO report of April 22, 1981 on "Factors Influencing DOD Decisions To Consent Activities for In-house To Contractor Performance" which concludes that "the most significant factor influencing decisions to convert from in-house to contractor performance was a cost savings identified by cost comparison. Personnel ceilings did not appear to be a factor even though the military services use DOD's CITA program to reduce their civilian personnel work force."

In a letter report to the Director of OMB dated September 30, 1981 (FPCD-81-77) the GAO recommended "To realize the full potential of the efficiency review program, we recommend that you require the military services to conduct efficiency reviews and develop and apply performance work statements for those commercial activities that must remain in-house." The GAO estimates that through implementation of the in-house reviews required by OMB Circular A-76 the DOD could save \$350 million annually, without letting a single contract - just improving in-house efficiency. In letter report FPCD-81-77 of September 30, 1981 the GAO recommended that OMB require wider agency usage of OMB guidelines in Circular A-76 on developing performance standards. And, in a letter report (PLRD-81-58) of August 26, 1981 to Mr. Addabbo, Chairman, Subcommittee on Defense of the House Appropriations Committee the GAO quoted the Defense Audit Service conclusion that "it did

not appear that contractors of CITA functions were bidding low and then unrealistically raising their prices."

This volume of analysis and investigation on the part of the GAO should not be overlooked in deciding how commercial and industrial support should be provided the VA. The very act which has been denied the VA by Congress, conducting Circular A-76 cost comparisons, results in sizeable savings. Our veterans deserve the best, most efficient care they can obtain. This Committee should be insisting on cost comparisons being conducted, not acquiescing in refusing them.

When a federal CITA function is put out for contract some 85% of the employees are retained in their jobs. Do they then become less efficient, competent or dedicated? Quite the contrary. Nothing so saps performance as working in an overstaffed, under-supervised environment. Circular A-767 requires that government employees be given first option on jobs contracted out, and they take full advantage to do so. Working in the private sector isn't all that objectionable to most Americans - in fact there are very few that don't work there before or after their government service. Almost all of our veterans are in the private sector, use to and content with the free enterprise system. In fact, if you query the veterans rather than the staff at VA facilities, I imagine you will find strong support for competitive, industrial care rather than bureaucracy.

Mr. Chairman, the thrust of my testimony is to not deny our veterans an opportunity for better, more efficient and less expensive care. It is depressing to see an arbitrary prohibition on cost comparisons to find out what savings would occur for our veterans through both reductions in in-house staff during the efficiency review and by contracting-out where it is cheaper. A-76 cost comparisons are working elsewhere in our government to save hundreds of millions of dollars. Don't do less for our veterans and our taxpayers.



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- ELECTRONIC INDUSTRIES ASSOCIATION
- HELICOPTER ASSOCIATION OF AMERICA
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- NATIONAL SECURITY INDUSTRIAL ASSOCIATION
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(303) 832-2800

STEPHEN M. SACKS
DIRECT LINE: (202) 872-6681

November 3, 1981

Dr. George A. Daoust
Executive Director
National Council of Technical
Service Industries
1850 K Street, N.W., Suite 1190
Washington, D.C. 20006

Dear George:

You have asked for our opinion as to whether a legal opinion issued by Guy H. McMichael, III, General Counsel of the Veterans Administration, to the Chief Medical Director of the Veterans Administration with respect to the contracting out of certain functions by the Department of Medicine and Surgery ("DM&S") is correct in light of the policies and procedures set forth in Office of Management and Budget Circular A-76. We have considered this opinion, as well as the legal authority cited by the VA General Counsel in his memorandum, and wanted to advise you that, in our opinion, the opinion of the VA General Counsel is an incorrect application of OMB Circular A-76.

The legal opinion by General Counsel McMichael takes the position that certain statutes dealing with missions and functions of the VA in the area of health care, as well as statutes dealing with the employment of civil servants, provide that the Department of Medicine and Surgery must perform all of its functions in house and cannot contract out any of such functions. It is interesting that, in reaching this conclusion, no specific provisions of these statutes are cited. Instead, the General Counsel has taken the position that, because statutes specify missions and functions for DM&S and certain other statutes deal with employment of civil servants by the VA, Congress intended there to be no contracting out of DM&S functions.

ARNOLD & PORTER

Dr. George A. Doust

Page Two

November 3, 1981

We disagree. Certainly, if Congress had provided a bar on contracting out (which Congress frequently does in certain specified circumstances), OMB Circular A-76 could not override that Congressional enactment. But, in the absence of such specified statutory language, we do not believe that the conclusions reached by the General Counsel with respect to the VA statutes is correct. Certainly, every federal regulation has statutes providing for the employment of civil servants. These statutes have expressly been held by numerous courts not to bar appropriate contracting out even where the functions performed pursuant to contract are similar to those performed by civil servants. Similarly, all federal agencies have statutes similar to those pertaining to DM&S which authorize those agencies to perform their basic missions. However, these statutes do not require that these missions be performed in one manner or another. Instead, resolution of that question is left to the discretion of Executive Branch personnel working under policy directives established by the President.

OMB Circular A-76, as revised, sets forth the clear policy of the Executive Branch with respect to the performance of functions by federal agencies. There is no mention in that circular of any exemption for the kinds of activities performed by DM&S. Indeed, Attachment A to Circular A-76, as revised on March 29, 1979, specifically lists a wide variety of health services, including "surgical, medical, dental and psychiatric care" and "hospitalization, outpatient, and nursing care" as "commercial and industrial activities" specifically covered by the policies in Circular A-76. As a result, many agencies have routinely contracted out medical functions where the other tests in Circular A-76 and its implementing regulations have been met.

ARNOLD & PORTER

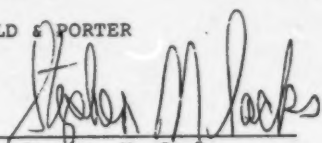
Dr. George A. Daoust
Page Three
November 3, 1981

Given the lack of any exemption in VA statutes, the clear policies in OMB Circular A-76 apply in our opinion to DM&S and mandate the use of contracting out where the other standards set forth in the circular have been met. For the foregoing reasons, we strongly disagree with the opinion issued by General Counsel McMichael with respect to the contracting out of functions by DM&S.

Sincerely,

ARNOLD & PORTER

By


Stephen M. Sacks



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

NOV 3 1981

Honorable S. I. Hayakawa
United States Senate
Washington, D. C. 20510

Dear Sam:

On October 28, 1981, I testified before the Joint Economic Committee on the Impact of Government Competition on Small Business. My testimony centered on implementation of OMB Circular No. A-76, which sets forth the Government's policy of reliance on competitive private enterprise for commercial or industrial products and services required by the Government.

We estimate that the Government currently operates thousands of commercial or industrial activities with an annual operating cost in excess of \$20 billion with a similar amount of capital investment. The vast majority of these activities has never been subject to competition. If these activities were subject to the cost comparison studies required by A-76, we estimate that as many as 154,000 personnel spaces could be converted to private sector contract operations with a 5-year cumulative savings between fiscal years 1982 and 1987 in excess of \$3 billion. These savings will continue to accrue thereafter.

The potential for such savings has been recognized for a long time. Since 1955, each Administration has expressed a general policy of reliance on the private sector for services needed to support the accomplishment of agency missions. The most recent expression of this policy was published in 1979. However, the policy has been applied unevenly over these Administrations, and it is now time to make it work.

Accordingly, the Reagan Administration would welcome a clear statement of intent by the Congress to support the policy that the Government should not compete with its citizens, and should rely on the competitive private enterprise system for needed goods and services. We, therefore, enthusiastically and fully support the Senate Joint Resolution 93, which you introduced on June 22, 1981. It is an excellent means to clarify and reaffirm this as a national policy and will illustrate to the public and private sectors alike that it is truly the Government's policy to rely on the private sector for needed commercial and industrial goods and services. The Resolution, provides timely support for President Reagan's quest for a new, revitalized approach to strengthening this country's economy. Economy and efficiency in Government and reward of the private sector for initiative and productivity are necessary ingredients in our formula for economic renewal.

Sincerely,

David A. Stockman

David A. Stockman
Director

Senator DECONCINI. Mr. Netterstrom.

Mr. NETTERSTROM. Mr. Chairman.

My name is James S. Netterstrom, CBSE. I am owner and president of Ship Shape Maintenance Co., Inc., a Washington, D.C. firm. I am also president-elect of Building Service Contractors Association International, which is headquartered in Vienna, Va. This statement is being submitted on behalf of the Building Service Contractors Association International.

BSCA International has 1,300 member companies, from 33 countries, with 90 percent in the United States. These companies are primarily engaged in providing cleaning services on a contract basis.

Our association strongly supports OMB Circular A-76 as being in the best interest of the Federal Government and the taxpayer. Cost comparisons between in-house cleaning and contract cleaning are very likely to indicate the Veterans' Administration could realize savings similar to those found in the Comptroller General's Report to the Congress, AFMD-81-78 relative to the cleaning costs of the General Services Administration. There is no factual basis to indicate that cleaning services provided by contractors would lower the quality of the services as now provided by VA employees. Hundreds of hospitals are currently being cleaned by contractors in all sections of the country, and many of these contracts have been in force with the same contractor for multiple years.

More than 80 percent of building service contractors employ non-union employees.

Contractors, particularly those providing cleaning services to hospitals, have the capability of providing services at any location. It is a common practice among building service contractors to have branch operations in multiple locations.

Those contractors who clean hospitals have proved that they have the capability to perform the highest level of cleaning. They have the necessary employee training and quality control to perform in accordance with job specifications.

Our association is dedicated to developing a high level of professionalism among its members. To this end, it has established extensive educational programs for executives, managers, and employees of building service contractors—including seminars, audio-cassettes, numerous monographs, a monthly magazine, an independent study program, a certified building service executive program, and a registered building service manager program.

Each of the latter two programs requires the successful completion of a full-day written examination to earn the designation, and each must be renewed every 3 years with the accumulation of professional development credits earned through continuing education. In addition, building service contractors cleaning hospitals employ certified executive housekeepers.

Our association respectfully requests that the VA and DM&S be required to implement the cost studies called for under OMB Circular A-76.

I'll be happy to answer any questions.

Thank you.

Senator DECONCINI. Thank you.

[The response of the Building Service Contractors Association International to written questions submitted by Hon. Alan Cranston, ranking minority member of the Senate Committee on Veterans' Affairs, follows:]

RESPONSE OF THE BUILDING SERVICE CONTRACTORS ASSOCIATION INTERNATIONAL TO
WRITTEN QUESTIONS SUBMITTED BY HON. ALAN CRANSTON, RANKING MINORITY
MEMBER OF THE SENATE COMMITTEE ON VETERANS' AFFAIRS

Question 1. Please provide for the record information as to the number of government hospital facilities at which your members have had contracts for cleaning over the past three years and the instances in which there have been work interruptions for all causes, such as strike, bankruptcies, contract defaults, and the like?

Answer 1. Our Association could survey its members to determine the number of government hospital facilities for which cleaning services have been contracted over the past three years, but it would require some time to gather this data. I feel sure that the contracting officers for each Federal agency have this information readily available and could supply it to you very quickly.

The various Federal agencies would also be in a better position to provide complete information relative to work interruptions. However, strikes are virtually non-existent in the building service contracting industry, and I have not heard of a single strike against a building service contractor cleaning a government hospital facility.

Question 2. Have any of the contracts which your organization has had with the federal government or medical facilities been terminated?

[If so] Why was the contract terminated? How many such contracts have been terminated?

Answer 2. Again, we could survey our members to ask them about the number of contracts for cleaning Federal Government and medical facilities which have been terminated and the reasons therefore. The various Federal agencies would be able to provide this information faster and more completely. Under the Services Contract Act, most Federal Government contracts are fixed-priced, low-bid, one-year contracts. Very few contracts are defaulted or performance bonds called by the Federal agencies.

We would welcome the opportunity to visit with you and discuss suggested revisions to the Services Contract Act which would be of long-term benefit to the Federal agencies and the taxpayers.

Question 3A. On a percentage basis, how many displaced government employees do you ordinarily hire when you receive a government contract for commercial or industrial type activities?

Answer 3.(a). The government employees involved in cleaning services are granted the right of first refusal by the contractor who assumes responsibility for providing those services. We could survey our members to determine the percentage of government employees hired by the succeeding contractor, but I doubt if such data would be readily retrievable from the personnel records of our member companies.

Question 3B. When you hire these employees, do you make any special efforts to give a preference to veterans?

Answer 3 (b). Building service contractors have generally found veterans to be preferred employees. Given a choice between a veteran and a non-veteran, with otherwise equal qualifications and attributes, a building service contractor would normally give preference to a veteran.

Senator DECONCINI. Thank you very much, gentlemen.

Now, Mr. Daoust, you made some reference regarding the PATCO incident, and, of course, I think that's the exception of Federal employees. It seems to me like most Federal employees don't strike, and they haven't in the history of our country. So I think that argument, with the exception of PATCO, does place, at least if you come to a conclusion that there is a sensitive area, and some, in my judgment, are, and many are not, areas, that there is some protection on having a law prohibiting strikes.

What kind of arrangements do you have with your employees regarding strikes?

Mr. DAOUST. Each situation varies, Mr. Chairman. I mentioned one that is rather critical, the last launch. It was perhaps very analogous. There was a small group of employees that thought they were absolutely key and essential to the Space Shuttle. They were employees of Boeing. They felt that if they did not have their demands met there was no way that Space Shuttle was going to be launched.

Just as the Federal Government did, Boeing worked right around them and served other people, and the launch went off at no problem.

A large responsible firm in the private sector is used to this sort of problem, and has continuously planned for it.

Senator DECONCINI. Can you give us any background on your—the organizations you represent? What is the history of strikes, with your employees?

Mr. DAOUST. It varies with company to company. With 25 million workers, it is the full gamut in labor relations, sir.

Senator DECONCINI. How about you, Mr. Pollard?

Mr. POLLARD. I'd be glad to give you our experience. We have been serving health-care now for over 20 years. I don't have the exact figure as to the number of hospitals that are unionized that we serve, but it is in excess of 180 of the 950. We have had no disruption in service as a result of strikes during that period of time.

I think it is also important again to emphasize, as I mentioned, we serve in many State and local governments, hospitals owned by State and local governments where there are similar provisions with respect to strikes. We are managing those employees. Those continue to be employees of the Government.

Senator DECONCINI. Let me compliment your company. I think that's an outstanding record of providing a service to what is a public need and being able to negotiate and manage without a disruption. There seems to be often greater public resentment of strikes when it deals with anything that is dealing with the Government than there is in the private sector, and I compliment your company for its fine record.

Has your company, Mr. Pollard, had any termination of contracts with the Government?

Mr. POLLARD. With the Government? The Federal Government?

Senator DECONCINI. The Federal Government.

Mr. POLLARD. Yes; we've had one termination of an Air Force hospital.

Senator DECONCINI. And when did that occur?

Mr. POLLARD. That would have occurred approximately 4 years ago. I do not have the exact date. That was a——

Senator DECONCINI. Was that a replacement with someone else?

Mr. POLLARD. No; that was a dispute over the terms of the contract and the scope of the service. That matter is still being reviewed.

Senator DECONCINI. And on a percentage basis, when you have been awarded a contract with the Government, how many displaced Government employees do you ordinarily hire when you receive the contract?

Mr. POLLARD. Well, I can give you the exact statistic on that, sir, submit it to the committee.

Senator DECONCINI. Would you supply that?

[See information furnished in response to written question No. 7 of Chairman Simpson, at p. 327 of this hearing record.]

Mr. POLLARD. But the fact that 90 percent has been quoted here several times, and that would generally be our experience. At the present time, as we are serving the Air Force, we are in the second generation, and it would certainly be the situation there.

Senator DECONCINI. Mr. Daoust, can you add anything to that statistic?

Mr. DAOUST. Yes, sir. We looked into it, through A-76 proposals. On the initial conversions it appears to run 85 percent of the separate employees will be hired. In some cases—I mentioned Fort Gordon which runs 96-plus. There is a very high correlation on the subsequent repeats, it runs even higher.

Senator DECONCINI. I'm sure you don't have the records here. Is it possible for you to put together the records of what kind of entry level salaries those people are hired at?

Mr. POLLARD. Yes; we certainly can have that. We can gather that information.

Senator DECONCINI. I'd appreciate seeing that if you could submit that to us.

Mr. POLLARD. I think, as our records would indicate here that it would be primarily historical data because of the Air Force does not have—we haven't had an Air Force contract every year, but we can certainly collect the data.

Senator DECONCINI. If you could give us a sampling of that, it would be helpful to the committee.

Mr. POLLARD. Sure, sure.

[See information furnished in response to written question No. 7 of Chairman Simpson, at p. 327 of this hearing record.]

Senator DECONCINI. If the VA did go to contracting out, say, in the maintenance area, and groundkeeping, there has been some success that has been demonstrated to me, at least in Arizona, and I am sure in other VA hospitals where it's very therapeutic and helpful to have some of the patients participate in those efforts, particularly long-staying patients.

Would that pose any problem of working with the contractor and the contractee to provide that kind of flexibility?

Mr. POLLARD. Well, I think we could respond to that need, and as again, as I indicated that in the majority of the hospitals we are serving in today—whether it's a private sector, in a private sector, we are managing the hospital's employees, and there are often cir-

cumstances which that hospital desires to maintain, certain employees in that function.

Senator DECONCINI. Do you have cases—any contract that you can think of where there is some program where a patient will participate for a period of time while he is there?

Mr. POLLARD. In some of the facilities, we have had that experience. We've also, as I cited, had other types of cooperative programs, as we did in one major Air Force hospital, where in fact the combination of our training program and their objective, over 30 people received their high school degrees. So that was not something that was done just by us, but it was done in cooperation with what the Air Force wanted to accomplish with respect to some of these entry-level employees.

Senator DECONCINI. Hypothetically, would you anticipate that altering a contract where you either made arrangements for education available, or permitted patients to have some participation in the maintenance and groundskeeping? Would you anticipate that that would raise the cost?

Mr. POLLARD. Yes.

Senator DECONCINI. And if you were doing it separately without those special arrangements?

Mr. POLLARD. Yes.

Senator DECONCINI. Do you have any idea to what extent?

Mr. POLLARD. No, it could vary so much. Senator, I wouldn't. It would have to be looked at under individual cases, but certainly to the extent that there was a factor which would mean that it would be less than a full productive man-hour, it would potentially raise the cost, yes.

Senator DECONCINI. I have no further questions. Do you have any?

We have some questions we would submit to you if you gentlemen would be so kind as to respond to them. It would help the full committee which, as you can tell, is not here today, and there may be several Senators, including Senator Simpson and Senator Cranston, that would ask you to respond to our questions.

We thank you very much for your very forthright and clear testimony this morning.

There being no further business to come to the committee, the committee will stand in recess subject to the call of the chairman.

[Whereupon, at 1:17 p.m., the committee was recessed subject to the call of the Chair.]

[The committee received the following letters, statements, and magazine articles for the hearing record:]

EDWARD ZORINSKY

NEBRASKA

481 RUSSELL SENATE OFFICE BUILDING
(202) 224-4381

COMMITTEE:

AGRICULTURE, NUTRITION, AND
FORESTRY

SUBCOMMITTEE:

RANKING MINORITY MEMBER
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ELECTRIFICATIONAGRICULTURAL PRODUCTION,
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STABILIZATION OF PRICES

FOREIGN AGRICULTURAL POLICY

United States Senate

WASHINGTON, D.C. 20510

FOREIGN RELATIONS COMMITTEE

SUBCOMMITTEE:

RANKING MINORITY MEMBER
WESTERN HEMISPHERE AFFAIRSARMS CONTROL AND
INTERNATIONAL OPERATIONS
EUROPEAN AFFAIRS

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LINCOLN, NEBR. 68508
(402) 471-82481811 WEST 2ND STREET
GRAND ISLAND, NEBR. 68801
(308) 381-7251

November 4, 1981

The Honorable Alan K. Simpson
Chairman
Committee on Veterans' Affairs
United States Senate
Washington, D.C. 20510

Dear Al:

I very much appreciate your agreeing to hold a hearing on November 5 on the issue of OMB Circular A-76.

The enclosed letters are representative of the many I have received from my constituents who are concerned about the possibility of contracting with private industry to provide services in VA medical facilities.

Those who wrote the letters which I have enclosed asked that they be included in the record of the hearing, and I would appreciate your doing so.

Again, many thanks for your concern and interest in this matter.

With best wishes,

Sincerely,


Edward Zorinsky
United States Senator

EZ/ek/mr

Enclosures

To: Senator Edward Zorinsky, D-Neb.
Room 431 Russell Building
Washington, D.C. 20510

From: Roger Freyer
11525 Westwood Lane #14
Omaha, Ne 68144
World War II Veteran
Korean War Veteran
DAVLife-Time member #295594--General MacArthur 2
Social Security number-485-12-3864

Subject: Senate Veterans Affairs Committee hearing Nov. 5

I would like to share with you sum of my observations that I have collected thru my being a patient and a volunteer at the VA Hospital, Omaha, Ne.; this has been collected over several years.

BUILDING MANEGMENT

Let me tell you that these people do more than sweep-swab floors and empty waste baskets. Along with their regular duties, they with only one or two exceptions, have acquired a "knack and/or rapport" with the patients, that they come in contact on a day to day basis. They show friendliness, concern in our general welfare. Willingness to help those who are to sick or can't walk, to get something from the canteen when they are their coffee-break. The list goes on. What I don't want should I ever be a patient again, is to have a stranger cleaning-up around me, kicking dust in my face.

DIETETICS

What makes up a good working department? I don't know, except they put-out good tasteey food and know how to serve it. Again, it is more than knowing to boil a pot of water or serving a tray. It's the people, who in their busy day, have a moment for US. No Saga contractor for me, building their profits and taking away from me!

CHAPLAIN

WHO would believe that this could possible happen, a contract with "WHO" for the services of a man-of-God. What will we have, a 8 to 5, 40 hourperweek WHO? WHO will be around when we need that soft word to keep us going or that final word so that we may 'go in peace'. Don't let them fool with this.

Ed, on my behalf and all others that feel the way I do about this contracting out of vital serves at any Nebraska VA Hospital, make those who suggest such a thing, prove that it will work. Not a "we'll try it for a year thing". And what about the people now in these jobs? Throw them out- no I don't think so!

Now comes the unions. They'll be along in all departments. The PATCO deal should be something for all of us to remember. With civilian employee's and unions, the management of each hospital will lose all kinds of control, even on a daily basis. And what about a strike that we patients would have no say in, what about us, our welfare?

There is so much more to tell in the wrong of this idea, I Pray that you will help those find the correct path.

Respectfully submitted,

A handwritten signature in dark ink, appearing to read "Roger Freyer". The signature is fluid and cursive, with the first name "Roger" written in a larger, more prominent script than the last name "Freyer".

Roger Freyer

October 29, 1981

George Brown
10-29-8

Honorable Senator Zorinsky

Washington D.C.

Dear Senator:

I am greatly concerned as to the contracting out of services in our V.A. health care system.

First of all, let me point out O.M.B. and David Stockman know nothing about the proper care for veterans' health care. Furthermore he is not a Veteran and does not care. I am referring to O.M.B. Circular A 76 on V.A. Health care system.

I sure outside contractors will go cheaper for the first time, till they get their foot in the door. Then prices will go up, & up, & up, with poorer service in the end. By that time the V.A. will have disposed of all our equipment and we are stuck to live with it.

The 30 million dollars could buy a lot of service for needy veterans. I am for cutting the budget, and here is a good place to start. Save 30 million.

The Circular violates Title 38. Title 38 is the public law governing the V.A., and guarantees the delivery of services to the V.A. health care program. O.M.B. and David Stockman have no knowledge or experience with the health needs, and care for veterans.

The V.A. network has maintained a good service to the veterans, nationwide for many years and let it be as it is. This study could

Cost 30 million dollars and prove nothing.
 Why spend that money, to investigate something
 that is doing a good job. Save the 30 million
 and spend it where it will do some good,
 some where else.

It is clearly against the law to contract out
 U. A. services. It is against Congress intentions,
 and veterans, and a good working U. A. system.

As a service officer for Disabled American
 veterans, Dist. I Nbr., I congratulate you for a
 good job you are doing. How you got into this I
 don't know. I know you know better. You are more
 intelligent than this.

I pledge to help you in any way I can. Please
 don't allow our services to be contracted out.

Sincerely I remain

Yours truly
 Lloyd K. Herfel

LLOYD K. HERFEL
 P. O. BOX 87
 GORDON, NE 69343
 308-282-0844
 DISABLED AMERICAN VETERANS
 SERVICE OFFICER

B.D. You may use this in your testimony Nov 5th
 Lloyd

March 29, 1981

March 25

Dear Senator Gounski:

Dear Senator Gounski:

When the Veterans Affairs Committee meets next month about changing Veteran Hospital kitchens to privately owned, please take these points into consideration. My husband is a service connected disabled Veteran, 100 %, since WWII he has been in and out of about 6 different VA Hospitals and the last 18 I have been right with him, I know the workings, good and bad of the VA Hospitals. The worst thing that could happen is to let a privately owned company take over the food department.

1. The employees could strike.
2. They would have no interest in the patients

2

3. In hospital employees and
facol. staff are honest.

We have both spent "time" in
 privately owned Hospitals and
 theft was a big problem
 among privately owned kitchen
 employees.

4. In the most part, the food
 is good at VA Hospitals,
 And as far time and the employees
 are always clean & neat & friendly.

Why Can't the government have
 good things alone? The VA
 Hospitals are needed and people
 who really care are needed.
 Don't change the VA Hospitals
 please. In privately owned
 facilities - they will get draft
 cigarettes, dippers, papers etc.
 They don't belong in a VA Hospital.

Sincerely,

Mrs. Gene Edwards.

CHAMBER OF COMMERCE
OF THE
UNITED STATES OF AMERICA

HILTON DAVIS
VICE PRESIDENT
LEGISLATIVE AND POLITICAL AFFAIRS

November 9, 1981

1885 H STREET, N.W.
WASHINGTON, D. C. 20062
202/889-6140

The Honorable Alan K. Simpson
Chairman
Committee on Veterans' Affairs
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

On behalf of the Chamber of Commerce of the United States and its over 191,000 members, I wish to express our views on Office of Management and Budget (OMB) Circular A-76 and its application to the provision of medical care by the Veterans Administration (VA).

We are greatly concerned by the provision in Title VI, Section 601 of the Veterans' Compensation Amendments of 1981 (P.L. 97-66), signed into law on October 16, 1981. We, like the Reagan Administration, find the provision very troublesome because it precludes the VA from conducting OMB Circular A-76 cost comparisons to determine the most economical mode of operation -- i.e., a contract or use of civil service employees. According to Administration estimates, "the application of this Circular to the VA's support-type hospital functions can result in an annual savings of approximately \$140 million, with no degradation in patient care." We agree.

Moreover, we take issue with the VA General Counsel's "legal opinion" in this matter -- i.e., VA's Department of Medicine and Surgery (DM&S) must perform all of its functions in-house and cannot contract out any of these functions. As we see it, Circular A-76 clearly applies to DM&S and mandates the use of contracting out where the other standards set forth in the Circular have been met. In fact, Attachment A to Circular A-76, as revised on March 29, 1979, specifically lists a wide variety of health services as "commercial and industrial-type activities" specifically covered by the Circular. Consequently, other agencies, such as the National Aeronautics and Space Administration, the Department of Defense and the Department of Health and Human Services, have contracted out medical functions. Therefore, in the absence of specific statutory language exempting VA, we conclude that the clear policies of Circular A-76 apply to VA and DM&S.

(over)

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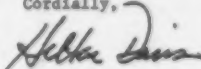
P

Y

The time has come to stop taking billions of dollars of work away from businesses, large and small -- those who pay a large share of America's taxes -- and to stop giving that work to federal employees whose facilities and salaries are paid for with those tax dollars.

I will appreciate your consideration of our views and I respectfully request that our letter and the enclosed statement on government competition be included in the hearings' record. The enclosed statement outlines the U.S. Chamber's strong support for vigorous implementation of Circular A-76 and government reliance on the private sector for needed goods and services.

Cordially,



Hilton Davis

Enclosure

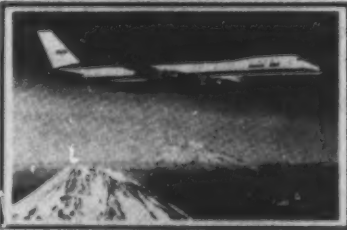
cc: Committee Members

Thomas E. Harvey, Majority Staff Director & Chief Counsel
Jonathan R. Steinberg, Minority Staff Director

CAMERA COPY—OFFSET



Statement of the
**CHAMBER OF COMMERCE OF THE
 UNITED STATES OF AMERICA**



STATEMENT
on
Government Competition (S.J. Res. 93, H.J. Res. 294)
for submission to the
SUBCOMMITTEE ON ADVOCACY AND THE FUTURE OF SMALL BUSINESS
of the
SENATE COMMITTEE ON SMALL BUSINESS
for the
CHAMBER OF COMMERCE OF THE UNITED STATES

by
Mark Schultz*
August 27, 1981

On behalf of the more than 158,000 members of the Chamber of Commerce of the United States, I wish to express our support for S.J. Res. 93 and H.J. Res. 294, joint resolutions which reaffirm the nation's longstanding procurement policy of government reliance on the private sector for needed goods and services.

The U.S. Chamber is the largest business federation in this country, representing more than 154,000 business firms, 2,700 chambers of commerce in this country and abroad, and 1,300 trade and professional associations.

A majority of these 154,000 business firms are small businesses. In fact, more than 97 percent of our member companies employ fewer than 500 persons, almost identical to the percentage of small businesses in the total economy. More than 60 percent of our members employ fewer than 20 persons, and more than 40% have less than 10 employees.

In view of these figures, it is fair to say that the U.S. Chamber represents the interests of American business, large and small, many of whom do business with the federal government. Accordingly, we clearly have a vital stake in eliminating government competition with the private sector in providing goods and services needed by the federal government.

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Federal Procurement Policy: Reliance on the Private Sector

The U.S. Chamber recognizes the significance of any proposed changes in federal procurement policy, which now involves more than one-tenth of the federal budget. Government procurement has a major effect on the nation's businesses, their employees, government employees, and on a broader level, all American taxpayers. The policies ultimately adopted not only affect immediately the expenditure of \$65 billion or more in taxpayers' money each year, but also guide the government's procurement activities for years to come.

In view of the above, it would be difficult for us to overstate the importance of close Congressional scrutiny of the total impact of any proposed changes to ensure that they do, in fact, contribute to the nation's longstanding policy of reliance on the private sector for needed goods and services.

Contracting Out vs. Government Competition

Competition with private industries by government agencies has been a source of increasing concern over the past few years.

According to recent General Accounting Office (GAO) estimates, federal employees currently perform 11,000 commercial or industrial activities that could be done by private firms. These activities cost taxpayers nearly \$19 billion last year.

Consequently, private firms are finding themselves increasingly competing not only with each other, but with the government as well -- at taxpayers' expense.

For a small business already burdened by spiraling inflation, high interest rates and excessive regulations, government competition is often a crippling blow.

A 1979 Small Business Administration (SBA) Task Force Report estimated that federal in-house activities in 1977 numbered 21,130, at an annual operation cost of nearly \$10 billion (a very conservative figure). According to this study, the best estimate is that at least \$2 billion annually might flow directly to small business if that \$10 billion were contracted-out in approximately the same proportion as other activities presently being contracted-out.

The Task Force also estimated the potential average annual savings to the taxpayer at \$2.98 billion. Clearly, small business is not the only likely beneficiary if federal in-house commercial or industrial activities can be reduced.

In sum, as the business community sees it, the "business of government is to govern," not to compete with its taxpaying constituents by hiring federal employees, whose salaries and facilities are paid for by taxpaying businesses, to perform industrial or commercial activities.

The service and support industries, particularly equipment and facility maintenance, are the hardest hit by government competition.
(See Appendix)

Some government agencies, having acquired surplus equipment and manpower, even sell services such as research and computer programming to other agencies.

This unnecessary growth of government competition undermines the private enterprise system and undercuts one of the nation's most valuable resources -- soundly conceived programs of scientific and technological research and development which have been vital to our economic growth, and to the welfare and security of our country.

History of Current Procurement Policy

The longstanding federal procurement policy has been, and continues to be, that the government should rely on the private sector for needed goods and services.

In 1932, the first study into the matter was made by a special committee of the House of Representatives. Numerous Congressional studies and commissions also have examined the problem in subsequent years.

However, our current procurement policy was not set forth until 1955, when the Eisenhower Administration issued a directive that the government should not provide services that put it in competition with private industry.

That policy was reaffirmed during the Johnson Administration by Circular A-76, issued by the Bureau of the Budget, predecessor of the Office of Management and Budget (OMB) (the Circular is now referred to as OMB Circular A-76).

Circular A-76 reiterated the government's general policy of reliance on the private enterprise system to supply its needs. It established the rule that goods and services were to be acquired from the private sector whenever feasible; the exception was to provide them in-house using federal employees.

Circular A-76 established new criteria for continuing or terminating in-house activity. It further provided that a government commercial or industrial activity may be authorized to provide goods or services only under certain conditions.

Advantages to Contracting Out

Circular A-76 was conceived in recognition of the major advantages of "contracting out" -- its cost-effectiveness, the flexibility it provides with regard to manpower and changing priorities, and its ability to increase technology transfers.

In most cases, the American taxpayer gets a much better deal under competitive contract than when functions are performed in-house. Procurement experts have estimated that competitive contracts can reduce costs by as much as 25 to 50 percent.

For example, according to the Office of the Secretary of Defense, for Fiscal Years '79, '80, and part of '81 DOD has conducted cost comparisons between in-house commercial activities and competitive contract performance. In 270 of these studies, contract performance was shown to be more economical and contracts were awarded, producing savings of \$209 million. In the other 158 cases, and with the incentives of job competition, in-house performance was shown to be more cost-effective, reducing costs by \$95 million.

Contracting out, besides being more economical, also provides government managers with a greater degree of flexibility. Contracts can be awarded, terminated, and reopened to provide needed goods and services at the lowest cost; not so with a government facility or work force. The very nature of government and bureaucracy, with the attendant civil service regulations, make reductions in force -- after a function is completed -- difficult if not impossible. While government priorities change and shift constantly, federal employees hired for one purpose remain on the government payrolls years after the project for which they were hired has been completed; not so with contracted employees.

Finally, when government research is performed by private firms, its application to civilian markets is accomplished more quickly. For example, the National Aeronautics and Space Administration's space program, which relies heavily on private sector research firms, has provided us with many useful consumer products.

It is essential that procurement policies and programs designed to further this progress in scientific knowledge and application take full advantage of the research capabilities and technical competency of private enterprise. Greater progress will be made by more fully utilizing the capabilities of private enterprise rather than by establishing or expanding government facilities in competition with them.

Implementation of Current Policy

However, as noted at the outset, over the past few years OMB Circular A-76's policy of reliance on the private sector effectively has been ignored.

Circumvention of this policy has been achieved through loose agency constructions of what is or is not a "governmental function." Under OMB Circular A-76, purely "governmental functions" are to be performed in-house. This exception to reliance on the private sector has provided agencies with "justification" for many of the activities performed by federal employees.

Threatened disruption, delays and degradation of service resulting from possible strikes by private sector unions is an often-cited reason for not contracting out important commercial or industrial functions. But, where strikes have occurred, rarely has degradation of service been experienced. Moreover, no longer can government union officials claim exemption from possible strike activity, in the wake of the threatened walk-out by postal officials and the actual strike by air traffic controllers.

Alleged abuses in the procurement system -- e.g., year-end spending, individual and organizational conflicts of interest, and sole-source contracting -- have led to calls for greater control over the so-called "beltway bandits" (i.e., consultants whose offices are located along the beltway surrounding Washington) and "invisible army of contracted employees." Unfortunately, this is a well-orchestrated movement which seeks to smear the private sector while expanding federal bureaucracy.

In fact, there is no sector of the economy with less control and accountability than government -- at all levels. Government accounting systems are oriented toward outlays and disbursements, not costs. No agency has a cost accounting system that rivals the cost accounting requirements for federal contractors. When an agency contracts for a product or service, there is a detailed accounting for all costs, in terms of the results provided. Conversely, when an agency performs a task in-house, there is control only over the number of employees and the total dollars expended -- but no control over, or accountability for, output.

Finally, critics of contracting out have made much of the large number of federal contractors and consultants. But the number of employees who may be involved in performance of federal contracts is immaterial; the fact that contract performance is more economical is the key point.

Preoccupation with the number of contract employees is irrelevant to the real issue -- economy in government. To begin with, there will never be a completely accurate account of contractors. Many are involved in providing the same product or service to private consumers; many contracts are awarded, and many others are completed each day. More significantly, most contracts are written in terms of the products or services to be provided and the cost to the government, not in terms of the number of people to be employed.

Federal Employee Union Pressure

Federal employee union pressure is most responsible for the current attitude toward contracting out.

These unions have taken a strong stance against contracts for work that could be performed by government employees. In addition, they have challenged the legality of "contract conversions", i.e., where a job previously performed by federal employees is contracted out, and have enlisted support from Members of Congress relative to agency decisions to award contracts.

The net effect of these lawsuits and protests is that agencies, understandably, are "gun shy" about awarding contracts or contract conversions.

The federal employee unions' tremendous influence has continued unabated because the business community and private sector unions have yet to exert a comparable countervailing influence.

Anti-Contracting Out Legislation

As a direct result of the federal employee unions' successful lobbying campaign, Congress over the past few years has placed moratoriums and more and more restrictions on contracting out. The Department of Defense (DOD) Appropriations Act for FY '78 contained a moratorium provision preventing contracting out of defense support functions.

In the 96th Congress, Section 502 of the DOD Authorization Act for FY '81 required detailed cost comparison studies which had to be certified by the Secretary of Defense and provided to Congress -- making

DOD's ability to convert work being done by federal employees to more cost-effective private contracts increasingly more difficult. The House version of the Act also contained a provision allowing federal employees the right to seek judicial review and relief when contract awards "adversely affected" their jobs.

Contractors also witnessed the introduction of a "federal employee relief bill" (H.R. 4717) by then-Representative Herb Harris which would have had a chilling effect on contracting out. The Harris bill was designed to prevent federal agencies from contracting out to avoid personnel ceilings. Agencies would be required to reduce their in-house personnel by the number of those contracted to perform a function. If it were found to be more cost-effective to perform a function in-house but the agency did not have the necessary personnel, the agency could request OMB to raise its personnel ceiling to accommodate the need.

Faced with the choice of losing personnel by contracting out or acquiring personnel by keeping work in-house, it is easy to predict what most agency managers would choose to do -- i.e., not contract out.

In the 97th Congress, Sections 602 and 304 of the House-passed version of FY '82 DOD Authorization (H.R. 3519) interfere with OMB Circular A-76 policies governing contracting out and conversion of DOD work to private contract. Section 602 would require military commanders to certify that a "contract conversion" would not jeopardize mobilization capabilities. Section 304 would prohibit the contracting out of an entire medical facility. Both provisions fly in the face of A-76 and would establish bad procurement precedents.

Section 10004 of this year's House budget reconciliation bill, as reported out by the House Post Office and Civil Service Committee, contained a recodification of the Harris proposal outlined above.

The Schroeder (D-Colo.) Amendment to the proposed Department of Energy (DOE) National Security authorization bill for FY '82 (H.R. 3413) would overturn a contracting out award made by DOE for security services at the Los Alamos National Laboratory in New Mexico.

Finally, the most subtle attacks on contracting out have been the constant allegations of contract abuses leveled at private consultants and a wide range of professional, research, and technical services, resulting in a variety of procurement "reform" bills.

These recent initiatives underscore the urgent need for Congressional action to reaffirm and codify the sound policy of reliance on the private sector.

Legislative Action

The Reagan Administration recently stated its position on contracting out, announcing full support for the same proven policy, i.e., reliance on the private sector whenever possible. The Administration further stated that correct and vigorous agency implementation of OMB Circular A-76 policy will give taxpayers what they deserve - economy in government.

In June, Senator S. I. Hayakawa (R-Calif.) and Representative David Dreier (R-Calif.) introduced joint resolutions to address the government competition problem.

S.J. Res. 93 in the Senate and H.J. Res. 294 in the House reaffirm and codify the time-honored, but erratically observed, policy embodied in OMB Circular A-76.

The Chamber wholeheartedly supports the Hayakawa-Dreier effort to help private contractors.

The time has come to stop taking billions of dollars of work away from businesses, large and small -- those who pay a large share of America's taxes -- and to ^{STOP} ~~start~~ giving that work to federal employees whose facilities and salaries are paid for with those tax dollars.

The U.S. Chamber appreciates this opportunity to address this important issue. I will appreciate your consideration of our views, and I respectfully request that this statement be included in the hearings' record.

APPENDIX

Where the Government Collides With Private Industry

Here is a sampling of industrial and commercial activities performed for the federal government by its own employees—

Agency and Activity	Number of Employees	Cost Per Year
Department of Energy, Washington, D.C., printing and binding	28	\$ 1,249,000
U.S. Coast Guard, Governor's Island, N.Y., maintaining golf course	6	\$ 45,000
Federal Aviation Administration, Oklahoma City, data-processing services	182	\$ 7,172,000
Federal Aviation Administration, Washington National and Dulles International Airports, janitorial services	60	\$ 1,004,000
Federal Railroad Administration, Alaska Railroad	474	\$37,000,000
Department of Energy, Portland, Oreg., power-systems operation	395	\$11,500,000
International Communication Agency, Washington, D.C., guard services	10	\$ 209,349
Federal Trade Commission, Washington, D.C., cigarette laboratory	7	\$ 200,000
Federal Trade Commission, Washington, D.C., micrographics	5	\$ 131,132
Veterans Administration, Department of Memorial Affairs, Farmingdale, N.Y., gravedigging and backfilling	23	\$ 512,000
Bureau of Engraving and Printing, Washington, D.C., ink manufacturing	40	\$ 4,000,000
Department of Justice, Justice Management Division, Washington, D.C., chauffeur services	10	\$ 277,165

Source: U.S. News & World Report

PREPARED STATEMENT OF STANLEY Q. LYMAN, EXECUTIVE VICE PRESIDENT, NATIONAL
ASSOCIATION OF GOVERNMENT EMPLOYEES

The National Association of Government Employees (NAGE) is grateful for the opportunity to present its views on the implementation of OMB Circular A-76 by the Veterans Administration to the Senate Committee on Veterans Affairs. We commend the Chairman and the Committee for focusing national attention on the problems associated with contracting out in the Veterans Administration. It is our hope that through these efforts, the American people will come to realize the danger which contracting out presents to the accomplishment of the mission of the Veterans Administration.

NAGE represents over 15,000 employees in the Veterans Administration and has long been opposed to wasteful, costly and unnecessary contracting out of government services. The evidence available at this time suggests that contracting out has cost the American taxpayers millions of dollars, has created enormous obstacles to accomplishing the missions of government, and has damaged morale in government to a dangerous extent. The evidence has not established that contracting out is a less costly way of accomplishing the aims of government as is suggested by its proponents.

Indeed, the General Accounting Office in a report issued on March 20, 1980, was roundly critical of the policies and practices of federal agencies in contracting out. The GAO stated that agency contracting practices had led to inefficient use of money and personnel, and a lack of agency control over the project. It was further noted that guidance provided by OMB in 1978 had led to little substantive improvement.

Despite all these concerns, the federal government's policy on contracting out has led to the growth of a huge shadow government. In the last decade, outlays for grants and contracts has grown astronomically, while at the same time, the number of official government employees has actually decreased. The number of employees under contract now exceeds civil service employees by over 70 percent.

The history of contracting out tells us that many agencies will contract out services which are unnecessary or could be more efficiently or effectively accomplished by in-house personnel. The considerable problems which arose with contracting out led OMB to revise circular A-76 in March 1979. This revision established procedures for determining when a function should be performed in-house by government employees and when it should be carried out under contract. However, the revised Circular A-76 has failed to provide adequate Federal guidelines on contracting out. This new document has failed to prevent the growth of this mammoth body of contracted employees, nor has it led to a more cost effective government as a result.

One of the primary reasons for the enormous growth of contracting out is the stated bias favoring contracting out which is prevalent in Circular A-76. The circular skews the requirement for cost comparison and calculation in favor of contracting out. This bias in favor of contracting out is shown by the fact that several contract related expenses are not even addressed. The Circular fails to factor the expense of unemployment payments, saved pay requirements, and placement and training programs for displaced civil servants. Nor does the cost calculation consider the effect on employee morale, and lessened productivity resulting from large scale reductions in force.

Several specific advantages are given to contractors in the Circular's provisions for cost comparisons. The methods of factoring in Federal retirement costs are blatantly unfair. In-house retirement costs are based on future as well as "length of contract" retirement costs. There is no equity in using a 20.4 percent of salary figure for in-house retirement costs when contractors are not required to use "dynamic normal cost projection" for figuring their retirement costs.

In addition, the Circular's provision for insuring cost comparisons based on efficient government operation of activities is particularly inadequate. Section 9.c.(1) reads: "Each agency should assure that Government operations are organized and staffed for the most efficient performance. To the extent practicable and in accordance with agency manpower and personnel regulations, agencies should precede reviews under this Circular with internal management reviews and reorganizations for accomplishing the work more efficiently, when feasible." There are too many qualifying phrases in the above provision. Further, given the inadequate enforcement provisions of the Circular, the above quoted provision has often been ignored by agencies which find it easier, even if ultimately more costly, to contract out work instead of tightening up their own operations. The victims in this scenario has been the American taxpayer who pays the unnecessary costs, and the patients of the Veterans Administration, who receive a lesser quality of services.

One of the most significant biases toward contracting-out reflected in Circular A-76 is the exemption from required cost comparisons of activities estimated at an annual cost of less than \$100,000. The revision of Circular A-76 raised the threshold for requiring cost comparisons by 100 percent: from \$50,000 to \$100,000. This provision, 9.a.(5), would exclude too many contracting decisions from cost comparisons.

In addition, it appears that agencies can divide an activity for contracting so that no contract is over the threshold. Such practices would save agencies the trouble of making cost comparisons. However, the American taxpayer, who ultimately pays for costly contracts, will have to foot the bill.

Section 9.a.(5) further provides that: ". . . Activities below this threshold (\$100,000), should be performed by contract unless in-house performance is justified in accordance with paragraph i.a. (Government Operation of Commercial or Industrial Activities: No Satisfactory Commercial Source Available) or 8.b. (National Defense.)" Amazingly, this provision does not even mention higher cost. Thus, not only are activities below the threshold exempt from cost comparisons, but they are also eligible for contracting-out regardless of expense. The revised guidelines give agencies carte blanche to engage in contracts under \$100,000.

Past experience tells us that agencies will take full advantage of this freedom to engage in costly contracts. The following is an example of the kind of abuse of sound fiscal principles that can be expected. The Langley Air Force Base in Virginia signed a contract with a private firm for painting the boiler room. The contract costs over \$40,000. However, because the contract fell below the \$50,000 threshold for requiring cost comparisons, no study

was made of the in-house cost of doing the job. The NAGE understands that the job could have been done in-house for \$16,000 to \$20,000. That is less than half the contract cost! This one example may sound miniscule when compared to an over \$500 billion Federal Budget, but it is indicative of the kind of irresponsible decision making that leads to excessive government spending and thus high taxes. Raising the threshold for cost comparisons to \$100,000 will only provide more opportunities for abusing federal monies.

Another glaring bias is the clearly deficient cost comparison requirement for contracts up for review. Under the guidelines, once contracts have been entered into, agencies have very little incentive to end them. The provision for the review of contracts, 10.c.(2) reads: ". . . The agency will review the contract cost and determine whether it is likely that the work can be performed in-house at a cost that is less than contract performance . . . When this is determined to be likely, a cost comparison will be conducted." (Emphasis added). In other words, agencies are not required to run cost comparisons during reviews of contracts unless the savings to be accrued through in-house operation are quite obvious.

NAGE finds the deficiency of the above requirement deplorable because recent pay caps mean that in-house operation of many activities may now be more cost advantageous than current contracts. It is unconscionable that Federal employees should have to suffer the effects of mandatory pay raise caps of 5.5 percent in FY 79 and 7 percent in FY 80 and 4.8 percent in FY 1981, then not reap the benefits of job security that would come from bringing contracted activities back in-house.

The evidence thus far has indicated that contractors tend to bid low in the first year. In subsequent years, the contractor is aware that administrators have no ability to reconvert the activity into an in-house operation since personnel slots are scarcer than dollars. The contractor is able to capitalize on the position he has the agency in, to extract exorbitant profit. A study done by the Department of the Army for the Health Service Command on the change in 23 custodial contracts at medical facilities from the first to the second year of the contract demonstrated a twenty-five (25) percent average increase in the cost of the contract. This increase was three or four times the rate of inflation at the time the study was done.

Not only are the guidelines biased toward contracting-out in the area of cost comparison, but the Circular is also deficient in the enforcement area. NACE is appalled at the lack of checks and balances on contracting-out decisions. The appeals provided for in the revised Circular are so limited that interested parties may not be able to stop a particular contract on the basis of excessive cost or a violation of the guidelines.

The Office of Federal Procurement Policy (OFPP), under OMB, has the authority only to review agencies' internal instructions and appeals procedures. The OFPP cannot review actual contracting-out decisions. The appeals procedures set forth in Circular A-76 does not authorize appeals outside the contracting agency. Agency determinations are not subject to negotiation, arbitration, or agreement. Even judicial review is prohibited. Appeals are only possible within the contracting agency, and the decisions of that agency are final. Yet, officials within the contracting

agency cannot possibly make impartial judgments.

The need for a substantially improved system of appeals on contracting-out decisions is dramatically illustrated by the fact that NAGE was unable to prevent a contract that is causing the needless expenditure of over \$2 million. In fall 1978, the Federal Aviation Administration (FAA) contracted with the Rockwell Company for the modification of 19 F/A Saberliner Aircraft. This work could easily be accomplished at the FAA's Air Service Base in Oklahoma City, Oklahoma, in nearly one third less time at a savings of approximately \$104,042 per aircraft for a total savings of about \$2,000,000. Despite the protests of NAGE and the Director of the Air Service Base, the bureaucracy within the FAA in Washington authorized and signed the Rockwell contract. This example clearly demonstrates that contracting-out decisions should be appealable to an independent party. The NAGE firmly believes that contracting-out decisions are of such significance that judicial review is warranted.

The revised OMB Circular has failed to eliminate the abuses of contracting-out. Indeed, the biased regulations concerning cost comparisons and inadequate provisions for reviewing contracts and appealing decisions has created a situation where graft and corruption in the award and administration of the contract can flourish. It is tragic to think that the quality of services provided to veterans could be diminished for this reason.

The issue in contracting-out is not solely one of cost effectiveness. Even if private industry is at times more efficient, can government afford to relearn part of its control over the function, and abdicate that responsibility to private

industry? NAGE believes that government should not relinquish its responsibilities to its veterans but rather should work to improve the efficiency and effectiveness of government services provided. It is suggested that the loyalty and dedication of career federal employees is more productive in servicing the needs of veterans than are private contractors whose motive is mere profit.

The Veterans Administration's mission of caring for veterans can more comprehensively be accomplished by a career federal employee, whether he be professional or blue collar, who has been instructed by hospital policy and regulation on the needs of the patient, and is willing to undertake that extra effort to support the agency's mission. The officials of NAGE have long been impressed by the dedication of VA workers in this regard.

When government functions are performed by government employees, the government retains managerial control of the employees and their work output. Government employees must maintain an acceptable level of job performance to qualify for within-grade salary increases, and employees who consistently perform at a less than acceptable level of job performance do not remain in their jobs. Management thus has tools to control and motivate the job performance of federal employees.

When work is performed by a private contractor, these management tools are not available. Employees of the private contractor are not subject to the federal personnel laws and regulations, and are not under the managerial control of government employees. In fact, Circular A-76 specifically prohibits the

establishment of an employer - employee relationship between the government and contracted personnel. Section 6- D(2) of the circular reads. "This circular will not be used as authority to enter into contacts which establish a situation tantamount to an employer-employee relationship between the government and contacted personnel...." Consequently control of government operations cannot be as thorough as the control to federal government can keep on it's own operation.

One of the most significant distinctions between the laws applicable to Federal employees versus those applying to private employees is the right to strike. The Civil Service Reform Act of 1978 did not give Federal employees the right to strike. Strikes are permissible under the National Labor Relations Act. The policies set forth under Circular A-76 fail to give agencies the freedom to reject a contract bid based on the possibility of a strike by contract employees. Section 8.1.(3)(d) reads: "The fact....that there is a possibility of a strike by contract employees is not an adequate justification for in-house performance of that activity. Urgency by itself is not an adequate reason for starting or continuing a Government commercial or industrial activity..." Consequently, under the new guidelines an agency could be forced to contract for products and services that would be delayed and even stopped due to job actions taken by private employees.

The contracting out of services is often a mask for a reduction in the level of services, which often could not be accomplished legislatively. Contractors are able to present

the agency with an attractive package of cost reduction by reducing the level of services. Inadequate investigation of the statement of work by the agency allows the contractor to achieve this result. In the interwoven environment of a veterans hospital any reduction in support on related services will have a domino effect impacting on patient care.

Many employees of the veterans administrations are themselves veterans hired pursuant to veterans preference consideration. A reduction in force will impact on the level of veterans employed in the agency, and put many veterans in unemployment lines.

The government's mandate to serve the public is not fulfilled when the wasteful, and capricious contracting out of it's functions lessens its efficiency unnecessarily using more of the public's tax dollar to provide them with less service. The Government exists to serve the public. When contracting-out serves to undermine that purpose by reducing the government's effectiveness, and increasing it's cost, it is time to drastically alter it's thinking in relation to contracting out. The criteria currently used to determine whether or not to retain a particular function in house harms the government, it's employees and the people it serves. The National Association of Government Employees urges this committee to consider legislation which would require that Veterans Administration give appropriate weight to the conditions outlined in our statement and control the growth of services contracted out by the Veterans Administration.

Contract housekeeping: hospital survey cites reasons for termination

BY JOSEPH D. BROWN, Ph.D.

HOUSEKEEPING

Based on a survey of a small group of hospitals, this article attempts to discover the reasons why hospitals have discontinued their contracts with outside firms in an effort to help hospital administrators avoid the pitfalls that can be associated with contracting for housekeeping services

Editor's Note

Turning over the day-to-day management of certain hospital departmental functions to an outside contractor is an alternative that has been available to hospitals for many years. If he thinks that it makes good management sense, today's administrator can negotiate agreements with contractors to provide services ranging from food to pharmacy to physical therapy.

Housekeeping was one of the first hospital services that outside contractors offered to provide, and the success of most such arrangements may be reflected in the large number of hospitals that currently delegate this service to others. According to the most recent (1975) American Hospital Association figures, no less than 11.9 percent of the nation's hospitals have come to accept contract housekeeping as a way of management life.

But contract housekeeping has not worked in all hospitals that have tried it—probably for as many reasons as there are variables within hospital and contractor organizations and in relationships between the two. The article that follows is based on a study that attempted to discover why a small group of hospitals that decided to try contracting for housekeeping services eventually discontinued the arrangement. It is presented for the purpose of helping hospital administrators who are considering such services to avoid the possible pitfalls that lurk in imprecise comparative costing, inadequate performance safeguards, and insufficient

controls. The reader should not infer that these experiences are in any way generally representative of results that might be expected with hospital contractors for housekeeping or any other hospital service.

The purpose of the survey that is described in this article was to determine why hospitals initially hired contract management firms for housekeeping services and why they later dismissed them.

A list was obtained of 74 hospitals that had hired and subsequently fired contract companies in recent years. These hospitals were dispersed throughout the United States and they varied in bed size from under 100 to more than 500, with more than half of the hospitals in the 100- to 249-bed range; nearly a third in the 250- to 499-bed range.

The study began in July 1980 with a letter to the administrator of each listed hospital. The letter explained the purpose of the survey and that the administrator or other individual who was responsible for hiring and terminating a maintenance firm would be telephoned to discuss the nature of their negative experience with contract housekeeping.

Of the original 74 administrators who were contacted, 12 were not interested in participating, 24 could not be reached, and 38 respondents were ready, willing, and able to take part. The findings reported here are based

on, and are subject to the limitations of, this admittedly small sample.

THE QUESTIONNAIRE

The first section of the questionnaire that was used for the telephone interviews asked why the outside contractor was hired and terminated, and each respondent was asked to explain the particular circumstances of their hospital. The second and final section contained 12 statements about the contract itself, operational factors, and the personnel who were provided by the contractor. Respondents were asked to agree or disagree with each statement and to rate—on a scale of 1 to 10—whether or not the contract company had delivered the services that it had initially promised to provide.

WHY THEY HIRED

The principal reason that was given for hiring a contract company by nearly half of the respondents was the inability of hospitals to find and to retain a good executive housekeeper. Secondary reasons for hiring an outside firm included expected cost savings, better quality housekeeping, and the availability of proven housekeeping methods and expertise. Other reasons that were given by a minority of administrators included their desire for fewer employee problems, the influence of other management people, an end to having to purchase maintenance supplies, expectation of good accountability of

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services rendered, better trained people, and cuts in administrative time.

A typical comment about hiring a contract firm was: "We listened to their sales story, and we felt a company could bring us a lot of support services that we couldn't afford ourselves. Secondly, we felt they would bring us experience in management that we just didn't have at the time. Third, they seemed to provide a sense of professionalism."

WHY THEY FIRED

The two main reasons given for the termination of contract services were a lack of cost-effectiveness and a lack of accountability. Additional reasons included poorer quality housekeeping, a lack of housekeeping control, the hiring by the hospital of a qualified supervisor, too much management turnover on the part of the contractor, failure to cut administrative time/supervision, and conflicts with the contractor's assigned executive housekeeper.

Administrators' comments about the cost-effectiveness of the contract services included: "It was not cost effective. The actual cleaning job was one of the key things. It just wasn't being done." And, "We felt that by eliminating the contractor we could decrease our costs by cutting out their management fee."

One administrator expressed the lack of accountability this way. "The hospital wasn't very clean. We had a lot of trouble and many patients complained. In addition, we didn't receive an effective response from the company when we would notify them of difficulties or problems."

Another respondent mentioned trouble over the contract agreement. "(We had) escalating costs in the contract that began to jump dramatically. We had a construction project going on, and as the contractor began to take over the responsibility of the new square footage, the contract was changed several times. We felt the changes were a little bit more than they were worth."

ADMINISTRATORS' ATTITUDES

Despite the foregoing negative comments, when administrators responded to questions about the contract in the second section of our question-

naire, most of them felt that the agreement itself was easy to understand. However, many respondents, (particularly from small hospitals) said that they were unable to identify specific costs in the contract for supplies, equipment, personnel, and the management fee. A majority of respondents agreed that the contract was easy to renegotiate as the hospital's needs changed.

More than three-quarters of the respondents gave negative answers when asked if the purchasing and infection control departments were free to select housekeeping products, and only half of the hospitals surveyed knew if legal counsel had reviewed the contract before it was signed.

Another administrator said the hospital had thought that certain levels of cleaning had been agreed upon, but when they analyzed the statements

in the contract, they did not conform with what had been verbally agreed upon.

OPERATIONAL FACTORS

In terms of operational factors, slightly more than half of the administrators felt that the contract company had met their housekeeping standards. On the other hand, more than half of all of the respondents indicated that other hospital departments were dissatisfied with the contractor's housekeeping services. A much smaller group felt that they had lost control over housekeeping functions. Both the dissatisfaction of other departments and the loss of control were problems more often felt by large hospitals than small ones.

When the respondents were asked if they had realized the savings that were predicted to result from the contract, 16 administrators said they did not save any money by employing an outside firm, 13 felt they had saved, and 9 others did not know.

CONTRACTOR PERSONNEL

When surveyed on their attitudes toward contractor personnel, a majority of hospitals said that as much time was spent administering the housekeeping function after the hiring of a contract firm as had been spent before. The same majority felt that the contractor's housekeeping personnel lived up to expected performance standards. Most of the respondents were satisfied with the firm's housekeeping director; however, more than one-half were dissatisfied with the high turnover rate among contractor-supplied housekeeping directors.

Following is one commentary on personnel problems. "We had some difficulty because of the fact that the housekeeping people did not feel that they were working for the hospital. They felt that they were working for someone else, and they were reluctant to take directions from us. Even though they were our employees, and only supervised by the outside firm, they immediately viewed that firm as being responsible for giving them directions."

In commenting on housekeeping management turnover, one adminis-

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trator felt that his hospital became a training ground, and that as a result, there was a lack of continuity in the services provided. Another said that if the hospital were to sign with another outside firm, the contract would have to spell out and guarantee the length of time a good manager would remain at the institution. A third said the firm's manager was good, but that the services delivered were of poor quality because hospital budgetary restrictions made it impossible for the manager to hire qualified personnel. Finally, the larger hospitals surveyed were less satisfied with the contractor's director of housekeeping than were smaller institutions.

CLOSING QUESTION

In seeking an overall opinion from the hospital administrators who were involved in the hiring and/or terminating of contract maintenance companies, we asked them to rate the degree to which the contract company had delivered the services that it had promised. On a scale of 1 to 10, the average rating that outside contractors received was 6.3.

In order to understand why some administrators rated the contract companies higher or lower than others, we measured each person's answer to the closing question against the responses they gave to each of the measured opinion areas in the questionnaire. The main reasons cited by respondents for giving companies lower overall performance ratings were the dissatisfaction of other hospital departments with the contractor housekeeping services and the administrator's feelings that the hospital was losing control over the housekeeping department. Other factors that contributed to low performance ratings were the failure to save money as predicted, dissatisfaction with the assigned director of housekeeping, and the feeling that the personnel who were hired by the contract company did not live up to the standards expected by the hospital.

Based on cross measurements of all of the survey respondents, it became clear that operational factors outweighed opinions about the contract itself or the personnel who were hired by the contractor when it came to forming a final judgment of the outside housekeeping company. ■

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